No. 06-1287
Title: CSX Transportation, Inc., Petitioner
v.
Georgia State Board of Equalization, et al.
Docketed: March 23, 2007
Lower Ct: United States Court of Appeals for the Eleventh Circuit
Case Nos.: (05-16000)
Decision Date: December 19, 2006
Rehearing Denied: February 12, 2007
Questions Presented

~~Date~~~	~~~~~~~~Proceedings and Orders~~~~~~~~~~~~~~~~~~~~~~~~
Mar 23 2007	Petition for a writ of certiorari filed. (Response due April 23, 2007)
Apr 23 2007	Brief of respondents Georgia State Board of Equalization, et al. in opposition filed.
May 7 2007	Reply of petitioner CSX Transportation, Inc. filed. (Distributed)
May 8 2007	DISTRIBUTED for Conference of May 24, 2007.
May 29 2007	Petition GRANTED.
Jun 19 2007	The time within which to file the joint appendix and petitioner's brief on the merits is extended to and including July 30, 2007.
Jun 19 2007	The time to file respondents' brief on the merits is extended to and including September 20, 2007.
Jul 25 2007	Blanket consent for the filing of amicus briefs in support of either party or neither party received from counsel for the petitioner and counsel for the respondents.
Jul 30 2007	Brief amicus curiae of United States filed.
Jul 30 2007	Joint appendix filed.
Jul 30 2007	Brief of petitioner CSX Transportation, Inc. filed.
Jul 30 2007	Brief amicus curiae of Association of American Railroads filed.
Jul 30 2007	Brief amicus curiae of Tax Foundation filed.
Jul 30 2007	Brief amicus curiae of Council of State Taxation filed.
Aug 17 2007	Statement of cost for printing the joint appendix received pursuant to Rule 26.
Aug 30 2007	SET FOR ARGUMENT Monday, November 5, 2007.
Sep 14 2007	Record received from U.S.D.C. for Northern District of Georgia. (4 boxes)
Sep 17 2007	CIRCULATED.
Sep 20 2007	Brief amicus curiae of Multistate Tax Commission filed.
Sep 20 2007	Brief of respondents Georgia State Board of Equalization, et al. filed.
Oct 4 2007	Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument filed.

Oct 15 2007	Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument GRANTED.
Oct 19 2007	Record received from U.S.C.A. for the 11th Circuit. (1 envelope)
Oct 22 2007	Reply of petitioner CSX Transportation, Inc. filed. (Distributed)
Nov 5 2007	Argued. For petitioner: Carter G. Phillips, Washington, D.C.; and Douglas Hallward-Driemeier, Assisant to the Solicitor General, Department of Justice, Washington, D.C. (for United States, as amicus curiae.) For respondents: Warren R. Calvert, Senior Assistant Attorney General, Atlanta, Ga.

SUPREME COURT U.S.
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OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION of the State of Georgia; Jerry Jackson, as Commissioner of Revenue of the State of Georgia; Russell W. Hinton, as State Auditor of the State of Georgia; and Ray J. Crawford, as Director of the Georgia State Properties Commission,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

PETITION FOR A WRIT OF CERTIORARI

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Avenue, NW
Washington, DC 20004
(202) 783-8124

JAMES W. McBRIDE
BAKER, DONELSON,
BEARMAN, CALDWELL
& BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

* Counsel of Record

March 23, 2007

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QUESTION PRESENTED FOR REVIEW

Whether, under the federal statute prohibiting state tax discrimination against railroads, 49 U.S.C. § 11501(b)(1), a federal district court determining the "true market value" of railroad property must accept the valuation method chosen by the State.

PARTIES TO THE PROCEEDINGS

Pursuant to Supreme Court Rule 14.1, petitioner states that all parties to the proceedings in the court whose judgment is sought to be reviewed are listed in the caption.

RULE 29.6 STATEMENT

CSX Transportation, Inc. has a parent company, CSX Corporation, which is publicly traded. No other publicly held company owns more than 10% of petitioner's stock.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner CSX Transportation, Inc. ("CSXT") respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eleventh Circuit in this case.

JUDGMENT FOR WHICH REVIEW IS SOUGHT

The opinion of the Eleventh Circuit is published at 472 F.3d 1281 (11th Cir. 2006), and is reproduced in the Appendix to this Petition ("Pet. App.") at 1a-23a. Its order denying rehearing is unpublished and is reproduced at Pet. App. 73a. The opinion of the United States District Court for the Northern District of Georgia is published at 448 F. Supp. 2d 1330 (N.D. Ga. 2005), and is reproduced at Pet. App. 24a-72a.

JURISDICTION

The judgment of the Eleventh Circuit was entered on December 19, 2006. Pet. App. 1a. The Eleventh Circuit denied rehearing on February 12, 2007. Pet. App. 73a. This Court has jurisdiction pursuant to 28 U.S.C. § 1254.

STATUTORY PROVISION INVOLVED

Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act" or "the Act"), 49 U.S.C. § 11501 (2002), is reproduced at Pet. App. 75a-77a.[1]

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[1] There are some differences in language between Section 306 as originally enacted in § 306 of Pub. L. No. 94-210, 90 Stat. 31, 54-55 (1976), and as subsequently codified at 49 U.S.C. § 11503 (which was later redesignated as 49 U.S.C. § 11501). The recodification, however, was not intended to effect any substantive change. *Burlington N. R.R.* v. *Okla. Tax Comm'n*, 481 U.S. 454, 457 n.1 (1987). Section 11501 has not changed since 2002, the year in which the dispute arose.

STATEMENT OF THE CASE

The opening sentence of the opinion below succinctly states the reasons why this Court should grant certiorari: "This appeal presents a question about state taxation of railroad properties that was expressly left open by the Supreme Court of the United States, has since divided the federal appellate courts, and involves the traditional balance of federal and state power." Pet. App. 1a. This Court should grant review to resolve the acknowledged 2-2 split among the circuits on whether, under a federal statute prohibiting discriminatory state taxes, railroads are permitted to prove the true market value of their property by appraisal methods different from those selected by the State.

Congress enacted Section 306 of the 4-R Act to prohibit, and to provide a federal remedy against, discriminatory state taxation of interstate railroads—a widespread and long-standing practice that Congress found seriously weakened the Nation's railroads and "unreasonably burden[ed] and discriminate[d] against interstate commerce." 49 U.S.C. § 11501(b). Eleven years later, in *Burlington Northern Railroad* v. *Oklahoma Tax Commission*, this Court held that Section 306's clear language plainly "permits review by federal courts of alleged overvaluation of railroad property by state taxation authorities." 481 U.S. 454, 456, 461 (1987).

Oklahoma Tax expressly identified, but left open, a question not presented in that case—whether a railroad could challenge the methodology used by a State to value its property in proving that state taxation authorities had overvalued the railroad's property. *Id.* at 465 n.5. The decision below, over a strong dissent, has deepened an already existing split among the circuits on this open question. At present, the Second and Ninth Circuits have held that railroads can prove the true market value of their property by using appraisal approaches different from those used by state taxing authorities, while the Fourth and Eleventh Circuits have held that railroads cannot

challenge the States' chosen methods. Certiorari is warranted to resolve this fundamental split of authority.

Moreover, the decisions of the Fourth and Eleventh Circuits ignore the clear language of the statute and frustrate the statute's fundamental purpose, which is to prevent discriminatory taxation of railroad property. By ignoring the clear intent of Congress, the decisions open a gaping loophole through which States can extract a disproportionate share of tax revenue from interstate railroads without fear of federal remedy. Indeed, there is already evidence that States in the affected jurisdictions have become increasingly aggressive in valuing railroad property. This Court's immediate intervention is imperative.

A. Statutory Background

Nearly 40 years ago, Congress recognized that interstate railroads "are easy prey for State and local tax assessors." S. Rep. No. 91-630, at 3 (1969). And, more than 30 years ago, after years of careful study, Congress determined that excessive and discriminatory taxation "by at least $50 million each year" contributed to the financial hardship that then plagued the railroad industry. H.R. Rep. No. 94-725, at 78 (1975).

Congress enacted the 4-R Act to address myriad problems that had left virtually the entire railroad industry in precarious financial condition and had resulted in eight major railroad bankruptcies. H.R. Rep. No. 94-725, at 53; S. Rep. No. 94-499, at 2-3 (1975), *reprinted in* 1976 U.S.C.C.A.N. 14, 15-17. Section 306 was a critical part of that reform, through which Congress intended "'to put an end to the widespread practice of treating for tax purposes the property of [railroads] on a different basis than other property in the same taxing district.'" S. Rep. No. 91-630, at 2.

Section 306 of the 4-R Act (hereinafter referred to as Section 11501, its present section within the U.S. Code) specifically outlaws four enumerated taxation practices of state and

local governments that "unreasonably burden and discriminate against interstate commerce," including:

> [a]ssess[ing] rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.

49 U.S.C. § 11501(b)(1).

This statute, which is the focus of this dispute, thus prescribes a precise formula for determining the existence of discrimination. Discrimination is measured by the ratio of assessments to "true market value," and the true market value of the railroad's property is a necessary factual finding that a district court must make in resolving a Section 11501(b)(1) claim.

Notwithstanding the Tax Injunction Act, 28 U.S.C. § 1341, Congress also granted federal district courts "jurisdiction . . . to prevent a violation of [Section 11501(b)]," but only "if the ratio of assessed value to true market value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." 49 U.S.C. § 11501(c). Finally, Congress specified that "[t]he burden of proof in determining assessed value and true market value is governed by State law." *Id.*

B. *Burlington Northern Railroad* v. *Oklahoma Tax Commission*

Eleven years after the 4-R Act became law, this Court granted certiorari to determine whether Section 11501 "permits review by federal courts of alleged overvaluation of railroad property by state taxation authorities." *Okla. Tax*, 481 U.S. at 456. This Court recognized that the 4-R Act's purpose was "'to provide the means to rehabilitate and maintain

the physical facilities, improve the operations and structure, and restore the financial stability of the railway system of the United States.'" *Id.* at 457 (quoting § 101(a) of the Act). Finding that "'railroads are over-taxed by at least $50 million each year,'" Congress chose to accomplish "the goal of furthering railroad financial stability" by prohibiting "discriminatory state taxation of railroad property." *Id.* (quoting H.R. Rep. No. 94-725, at 78). This Court acknowledged that Section 11501 was "Congress' solution to the problem of discriminatory state taxation of railroads." *Id.*

This Court stated that "the language of § 11503 [now § 11501] plainly declares the congressional purpose," holding that "[i]t is clear from this language that in order to compare the actual assessment ratios, it is necessary to determine what the 'true market values' are." *Id.* at 461. Although the court of appeals in that case had "found that its restrictions on valuation actions under § 11503 [now § 11501] [were] necessary in order to avoid 'an inevitable clog of federal dockets' and 'unreasonable delay of the state tax collection process,'" *id.* at 464, this Court rejected such considerations, stating:

> These are policy considerations which may have weighed heavily with legislators who considered the Act and its predecessors. It should go without saying that we are not free to reconsider them now.

Id.

In passing, this Court briefly explained in a footnote an issue that had not been presented by petitioner and left that issue open for resolution another day:

> Petitioner has not challenged the valuation methodology employed by respondents in determining the value of petitioner's railroad; petitioner's sole challenge is to the application of that methodology . . . . This case therefore does not present the question whether a railroad may, in an action under [Section 11501] challenge in the district court the appropriateness of the accounting

> methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied. Accordingly, we express no view on that issue.

Id. at 463 n.5.

C. Factual Background

This case involves CSXT's challenge to the 2002 valuation of its property by the State Board of Equalization of Georgia ("the Board"), and raises the issue left open in *Oklahoma Tax*. Under Georgia law, most commercial and industrial property is locally assessed by county boards, but public utilities (including railroads) are centrally assessed by the State. Georgia counties are permitted, but not required, to use the State's proposed assessment for each county in imposing taxes. Pet. App. 2a-3a.

In Georgia, the Property Tax Division of the Georgia Department of Revenue ("the Department") prepares assessments for review and approval by the Board. In 2002, as in prior years, the Department calculated the market value of all public utilities using the unit rule. Under the unit rule, the value of the railroad as a whole is calculated, and the Georgia portion of that property is determined by multiplying the unit value by the percentage of CSXT rail miles in Georgia. Pet. App. 3a.

In 2002, the State's appraiser changed the valuation methods that the Department used to calculate value under the unit rule. Formerly, the Department used a yield capitalization method (an income approach), a direct capitalization method (an income approach), and a stock-and-debt method (a sales comparison approach). Each method generates a value that could be compared to the others. For the 2002 tax year, the appraiser replaced the first two of those methods with a discounted cash flow ("DCF") method (an income approach) and

a market multiples method (a sales comparison approach). Pet. App. 4a.

The appraiser generated five values from these approaches, ranging from $8.126 billion (using the DCF method) to $12.346 billion (using the market multiples method). Pet. App. 4a. The appraiser selected a unit value of $8.2 billion as close to the lower of his estimates.[2] *Id.* at 5a. The appraiser's 2002 overall unit value for CSXT of $8.2 billion was 47.1% higher than the 2001 valuation. *Id.* at 62a. After adjustments and deductions, the appraiser calculated taxable market value of CSXT in Georgia (based on the percentage of rail miles in the State) at $514.9 million. *Id.* That was an increase of 36.3% from the 2001 Georgia taxable value. Moreover, the 2002 taxable value would result in an increase in CSXT's property tax liability in Georgia to $6.5 million, whereas its 2001 liability was only $4.6 million.

D. Proceedings Below

1. *The District Court.* CSXT filed a complaint in the United States District Court for the Northern District of Georgia challenging the Department's valuation under Section 11501 of the 4-R Act. Pet. App. 5a.

CSXT argued that the proposed valuation violated Section 11501(b)(1) because the Railroad's true market value was $6 billion, not $8.2 billion, and thus "it was taxed at a higher ratio of assessed value to true market value than other commercial and industrial property." Pet. App. 7a. CSXT submitted an appraisal prepared by a valuation expert, Thomas Tegarden, whose credentials were described by the district court as "'impeccable.'" *Id.* (quoting 448 F. Supp. 2d at 1333). Tegarden used three different methods to approximate "true market value," but relied primarily on a yield capitalization approach. *Id.* at 7a-8a. Based on a unit value of $6 billion, he

[2] Georgia's 2002 unit value of $8.2 billion was the highest among the 15 States where CSXT operates that use the unit value method. Tr., vol. 11, at 578.

calculated the value of CSXT's Georgia property as worth $369.3 million. *Id.* at 25a.

The district court held that it was not permitted to consider Tegarden's appraisal because the 4-R Act barred consideration of appraisals "based on a valuation methodology different from the methodology used by the State, unless the methodology of the State is irrational or intentionally discriminatory." Pet. App. 7a. The district court elaborated:

> This is a case brought under the 4-R Act and the court must determine the true market value of CSXT. *CSXT, in turn, has the burden of proving by a preponderance of the evidence that the true market value of its property is $6 billion.* To do this, CSXT presented two types of evidence. First, it criticized the Department's calculations. Second, it presented a valuation of its property by Mr. Tegarden. *In a more typical case, the court would look to both Mr. Tegarden's appraisal and the Department's appraisal to determine the true market value of CSXT.* If the court found by a preponderance of the evidence that CSXT's true market value was $6 billion, as proposed by CSXT, then the court would compare the Department's Proposed Valuation to CSXT's true market value to determine if discrimination occurred. *However, as explained later in this order, the court cannot consider Mr. Tegarden's valuation because it was prepared using different valuation methods than the Department. The court, therefore, is limited to looking solely at CSXT's criticisms of the Department's valuation.*

Id. at 37a n.8 (emphases added).

The district court further rejected CSXT's argument that Tegarden's valuation methodology was a variant of the State's own methodology. Pet. App. 45a. Finally, the district court rejected CSXT's challenges to the Board's calculations, and found that the unit value of CSXT's property was $7.7

billion, and therefore the ratio of assessed to market value of CSXT's property did not exceed by more than 5% the same ratio for other commercial and industrial property. The district court accordingly entered judgment for the Board. Pet. App. 48a.

2. *The Eleventh Circuit.* A divided court of appeals affirmed. The court began by stating that "[w]hether a railroad may challenge, under the 4-R Act, the valuation methodology of a state is a question the Supreme Court has acknowledged but not decided." Pet. App. 9a (citing *Okla. Tax*, 481 U.S. at 462-63 & n.5). The Eleventh Circuit then expressly recognized a circuit split:

> Three of our sister circuits, following *Burlington Northern v. Oklahoma*, have split on whether railroads may challenge state valuation methodologies. The Fourth Circuit, on the one hand, has concluded that the 4-R Act does not permit a railroad to challenge the valuation methodology of a state. That circuit concluded that the text of the Act is ambiguous, and the court was "not inclined to disregard" the general policy of noninterference in matters of state taxation contained in the Tax Injunction Act "where § [11501] does not plainly authorize such an exception." *Chesapeake W. Ry. v. Forst*, 938 F.2d 528, 531 (4th Cir. 1991); *accord Richmond, Fredericksburg & Potomac R.R. Co. v. Forst*, 4 F.3d 244, 250 (4th Cir. 1993). The Second and Ninth Circuits, on the other hand, have repudiated *Chesapeake Western* and held that railroads may challenge valuation methodologies. In *Burlington Northern Railroad v. Department of Revenue*, the Ninth Circuit explained that section 11501(c) of the 4-R Act provides that state law governs the burden of proof in challenges to assessed value and true market value. 23 F.3d 239, 241 (9th Cir. 1994). Because determinations of property value by public officials in the State of Washington may be defeated by "clear, cogent and convincing evidence," the

> court reasoned that state valuation methodologies may likewise be defeated by clear, cogent, and convincing evidence. *Id.* In *Consolidated Rail Corp. v. Town of Hyde Park*, the Second Circuit held that, at least where states use a unique method to appraise railroads, the 4-R Act allows railroads to challenge valuation methodology. 47 F.3d 473, 482 (2d Cir. 1995).

Id. at 10a.

The Eleventh Circuit sided with the Fourth Circuit, applying the "clear statement rule" of *Gregory* v. *Ashcroft*, 501 U.S. 452, 460-61 (1991). Pet. App. 11a-12a. Citing *Department of Revenue* v. *ACF Industries, Inc.*, 510 U.S. 332 (1994), which involved a different subsection of Section 11501, Pet. App. 13a-14a, the court found no clear statement that railroads could challenge the methodology by which the valuation was made.

The court also rejected the argument of CSXT and *amicus curiae* Association of American Railroads "in the alternative, that the appraisal by Tegarden was based on the same methodology used by the State" and represented merely a different approach to applying the same "unit rule" methodology. Pet. App. 15a. The Eleventh Circuit interpreted the Supreme Court in *Oklahoma Tax* as drawing a distinction between "accounting methods" and "factual determinations," and the court below held that the former encompassed "all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be." *Id.* at 16a-17a. The railroad could not contest any such nonfactual determinations in proving "true market value" under Section 11501(b)(1).

Judge Fay concurred in part but dissented with regard to "the majority's holding that the 4-R Act bars the Railroad from challenging the valuation methodology chosen by the state," agreeing with the majority that "our sister circuits have split on this issue." Pet. App. 20a. Judge Fay declared that

"[t]he language of the statute is straightforward and prohibits states from assessing rail transportation property at a value that has a higher ratio to the true market value than the ratio that the assessed value of other commercial and industrial property has to its true market value." *Id.* Judge Fay concluded:

> Since the objective of any methodology is a determination of true market value, a railroad should be allowed to challenge the method used in an attempt to prove that the result of such a method was not the true market value of its property. . . . If the Railroad can prove that the method used by the state does not result in a fair appraisal of true market value and that the assessed value is in fact at a ratio higher than five percent of the ratio of true market value and assessed value of other commercial and industrial property, it is entitled to relief.

Id. at 23a.

REASONS FOR GRANTING THE PETITION

This Court should grant the petition to resolve a clear and acknowledged conflict among the circuits over whether railroads may challenge the State's methodology in proving "true market value" under the 4-R Act. Since *Oklahoma Tax* identified the issue, courts of appeals have hopelessly divided in grappling with it. The Second and Ninth Circuits have properly ruled that railroads can prove the "true market value" of their property by use of appraisal methods different from those employed by the state tax authorities. In contrast, the Eleventh Circuit (in the decision below) and the Fourth Circuit have ruled that railroads may not challenge state methodologies in satisfying their "true market value" burden. Indeed, the Eleventh Circuit has gone the farthest of any court, eviscerating the discrimination protections of the Act by immunizing from federal court review "all nonfactual determinations involved in constructing a valuation process, regard-

less of how broad or narrow they may be." Pet. App. 16a-17a.

The Fourth and Eleventh Circuit's holdings are wrong because they cannot be reconciled with the plain language of the statute and with any meaningful policy of protecting railroads against discriminatory taxation. Section 11501 prescribes a precise formula for measuring discrimination. Under that formula, true market value is the economic standard by which the existence and degree of discrimination is determined. If States are free to define unalterably the methods by which the true market value of railroad property may be proven in court, railroads will be severely prejudiced in proving discrimination under the statute.

Moreover, such incorrect decisions create perverse incentives for States to pick methodologies that artificially inflate railroad property values. Indeed, there is already evidence that States are becoming more aggressive in their valuations of railroad property. See *infra*, at 19-22. Accordingly, this Court should grant review.

I. THE DECISION BELOW DEEPENS AN ALREADY EXISTING SPLIT AMONG THE CIRCUITS REGARDING THE RAILROADS' ABILITY TO CHALLENGE STATE METHODOLOGY.

As the Eleventh Circuit acknowledged (Pet. App. 10a, 13a-14a; *supra* at 9-10), there is a 2-2 split among the courts of appeals on the question left open by *Oklahoma Tax*:[3] whether

[3] It is notable that the Department of Justice, in a brief filed by the Solicitor General in the *Oklahoma Tax* case, has already advised this Court of its position that Section 11501(b)(1) permits challenges *both* to the methodology and to application of the methodology: "Section [11501] prohibits any overvaluation of railroad property that results from an assessment rule or *methodology* that—*either on its face or as applied*—systematically determines excessive values for railroad property." Brief for the United States as *Amicus Curiae* in Support of Petitioner at 12, *Burlington N. R.R.* v. *Okla. Tax Comm'n*, 481 U.S. 454 (1986) (No. 86-337) (internal quotation marks and citation omitted) (emphasis added).

the railroad may fully adjudicate its true market value as part of its Section 11501 case by challenging the State's methodology. The Eleventh Circuit joined the Fourth Circuit in ruling that railroads may not prove true market value of railroad property except by the valuation methods the State employs. In stark contrast, the Second and Ninth Circuits have ruled to the contrary. This Court should resolve the mature and expanding conflict.

1. *Fourth Circuit.* The first court of appeals to address the issue left open by *Oklahoma Tax* was the Fourth Circuit. In that case, the plaintiff-railroads contended that "Virginia's valuation method for railroad property impermissibly discriminates against railroads by valuing railroad property in excess of its true market value." *Chesapeake W. Ry.* v. *Forst*, 938 F.2d 528, 529 (4th Cir. 1991). Rejecting the plaintiff-railroads' claim, the court of appeals explicitly held that "challenges to state valuation methodologies are not cognizable under § [11501]." *Id.*

The court of appeals explained that there were two methods of valuation in dispute in the case: "inventory and summation" and "unit method." *Id.* When Virginia replaced the unit method with the inventory and summation method, the plaintiff-railroads brought suit, "charging that valuation of railroad property under the inventory and summation methods results in such property being assessed at a greater than true market value." *Id.* at 530.

Specifically, the court concluded:

> § [11501] does not provide a basis for railroads to challenge a state's preferred methodology for ascertaining the true market value of railroad property. The statute simply does not authorize the judiciary to enter into the difficult task of second-guessing a state's policy assessment of how best to value property. In light of Congress' expressed preference against federal interference in state taxation policy, we believe that § [11501] should

> be read narrowly, authorizing challenges to a state's calculation of fair market value, but not to a state's method for calculating such value. . . . The 4-R Act does not authorize the judiciary to undertake the difficult, and arguably impossible, task of determining which specific assessment methodology produces true market value of railroad property.

Id. at 533.

Although the Fourth Circuit later made clear that a plaintiff-railroad could file suit challenging the *application* of the State's methodology, it reaffirmed its holding in *Chesapeake Western* that "'§ [11501] does not provide a basis for railroads to challenge a state's preferred methodology for ascertaining the true market value of railroad property.'" *Richmond, Fredericksburg & Potomac R.R. v. Forst*, 4 F.3d 244, 248-49 (4th Cir. 1993) (quoting *Chesapeake Western*, 938 F.2d at 533); see also *id.* at 250 ("Although a plaintiff railroad must accept a state's chosen methodology, § [11501] does not require that it accede to the state's application of that methodology.").

2. *Ninth Circuit.* The second court of appeals to address the issue was the Ninth Circuit, which expressly disagreed with the Fourth Circuit's reasoning. There, the plaintiff-railroad argued that the district court had "wrongly relied" on *Chesapeake Western* in "deferring to the state's choice of the valuation method used to set the market value of its property." *Burlington N. R.R.* v. *Dep't of Revenue*, 23 F.3d 239, 240 (9th Cir. 1994). The Ninth Circuit explained that *Chesapeake Western* had held that "although a railroad may challenge the application of the valuation method used by a state, it cannot challenge the method itself." *Id.*

The Ninth Circuit stated that it "need not decide whether *Chesapeake Western* should be followed in this circuit," *id.*, for the district court had not precluded the plaintiff-railroad "from challenging the state's method of valuation," but in-

stead had allowed the railroad "to present evidence of the railroad's value based on other valuation methods." *Id.* Importantly, the court of appeals held that it was "proper" that "the district court did not blindly accept the state's valuation method. It simply gave substantial deference to it" under Washington state law, where "the determination of the value of the property by public officials is presumed correct" and "[t]his presumption may be defeated only by evidence that is 'clear, cogent and convincing.'" *Id.* at 240-41 (quoting RCW 84.40.0301(1)); see also *id.* at 241 (holding that the district court had "correctly applied" the Washington law standard).[4] The Ninth Circuit rule, as summarized by the court below in rejecting it, is that "state valuation methodologies may . . . be defeated by" expert valuation evidence satisfying the applicable standard of proof. Pet. App. 10a.

3. *Second Circuit.* The Second Circuit then deepened the existing split between the Fourth and Ninth Circuits. The court recognized that in its case, the "controversy stems primarily from the difference in appraisal methods. The [State] had used the 'cost approach' method for determining true market value, while [the plaintiff's] experts have applied both the 'income capitalization method' and the 'stock and debt' method." *Consol. Rail Corp.* v. *Town of Hyde Park*, 47 F.3d 473, 480 (2d Cir. 1995).

"Relying primarily on" *Chesapeake Western*, the State in *Hyde Park* argued that the plaintiff-railroad was "bound by the method of appraisal the [State] ha[d] chosen, and that the court could not "consider any other method of valuation in fixing the 'true market value' of" the plaintiff-railroad's properties. *Id.* at 481-82. The Second Circuit explicitly rejected the *Chesapeake* court's view that "the method of appraisal as a matter of state policy . . . was beyond the reach of the 4-R

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[4] Section 11501 provides that "[t]he burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. § 11501(c).

Act," holding unequivocally, "[w]e do not accept that interpretation of the statute." *Id.* at 482.

4. *Eleventh Circuit.* CSXT urged the Eleventh Circuit to steer clear of the error of the Fourth Circuit's *Chesapeake Western* decision, arguing that the income approach used by its appraiser was the same income "method" used by the State's appraiser. CSXT C.A. Reply Br. at 14-17. The Eleventh Circuit rejected that argument, sided with the Fourth Circuit on the methodological issue, and acknowledged a conflict with the Second and Ninth Circuits. Pet. App. 10a, 13a-14a. See *supra* at 9-11 (discussing decision below).

II. THE DECISION BELOW DIRECTLY CONTRAVENES THE PLAIN LANGUAGE OF THE STATUTE AND UNDERMINES THE FEDERAL ANTI-DISCRIMINATION REMEDY.

The mature and acknowledged 2-2 circuit split alone warrants issuance of the writ, but this Court's intervention is all the more imperative given the Eleventh Circuit's critical error in interpreting Section 11501 on this important and recurring issue of federal law.

The Eleventh Circuit's myopic interpretation of Section 11501(b)(1) cannot be reconciled with the plain language of the statute. The entire "true market value" of the railroad is an element of a Section 11501(b)(1) claim and a matter to be resolved by the courts; as this Court explained, "[i]t is clear from this language that in order to compare the actual assessment ratios, it is necessary to determine what the 'true market values' are." *Okla. Tax*, 481 U.S. at 461. True market value is a question of fact on which the railroad bears the burden of proof, 49 U.S.C. § 11501(c), and there is nothing in the statute that commands the trier of fact to defer to a state tax agency's choice of valuation methods.

A federal court cannot accomplish its statutory mandate of determining the ultimate fact of "*true* market value" if it is hamstrung by the Eleventh and Fourth Circuits' rule that the

reviewing court must accept the State's valuation methodology. As this Court recognized in *United States* v. *Miller* concerning the Just Compensation Clause, in the absence of a functioning market that prices the property, a jury determination of "fair market value" necessarily "involves the use of assumptions, which make it unlikely that the appraisal will reflect true value with nicety." 317 U.S. 369, 374 (1943). Even if the determination of overall "fair market value" in such circumstances is but "a guess by informed persons," *id.* at 374-75, it is still necessarily a question of fact within the fact finder's province, to be decided based on all relevant evidence. As the district court here recognized, that is the standard practice in every proceeding in which a property's market value is at issue. Pet. App. 37a n.8; *supra* at 8. As the Ninth Circuit has recognized:

> Complex factual inquiries such as valuation require the trial judge to evaluate a number of facts: whether an expert appraiser's experience and testimony entitle his opinion to more or less weight; whether an alleged comparable sale fairly approximates the subject property's market value; and the overall cogency of each expert's analysis. Trial courts have particularly broad discretion with respect to questions of valuation.

Ebben v. *Commissioner*, 783 F.2d 906, 909 (9th Cir. 1986) (determination of "fair market value" under federal tax laws). Congress clearly intended district courts to determine the "true market value" of railroad property with the aid of expert testimony, including expert testimony on appropriate valuation methods.

Thus, even if a "clear statement" were required, Congress's mandate that federal district courts determine the "*true* market value" of railroad property in resolving a claim of discriminatory property tax assessments amply suffices. See 49 U.S.C. § 11501(b)(1). Regardless, the Eleventh Circuit's invocation of the "clear statement rule" is improper. The court relied on *Department of Revenue* v. *ACF Industries, Inc.*, 510 U.S. 332

(1994), but that case raised a much different question under the 4-R Act. At issue in *ACF* was subsection (b)(4), which prohibits "another tax that discriminates against a rail carrier." 49 U.S.C. § 11501(b)(4). The question presented was "[w]hether a tax upon railroad property is even subject to challenge under subsection (b)(4) on the ground that certain other classes of commercial and industrial property are exempt." 510 U.S. at 339-40. This Court recognized that "Congress did not state whether exemptions are a form of forbidden discrimination against rail carriers, and further did not provide a standard for courts to distinguish valid from invalid exemption schemes." *Id.* at 343. This Court consequently held that § 11501(b)(4) "does not limit state discretion to levy a tax upon railroad property while exempting various classes of nonrailroad property." *Id.*

However, in recognizing this ambiguity of subsection (b)(4), this Court reiterated that Congress's intent was clear in subsections (b)(1) through (b)(3):

> *The reach of subsections of (b)(1)-(3) is straightforward:* These provisions forbid the imposition of higher assessment ratios or tax rates upon rail transportation property than upon "other commercial and industrial property." The scope of subsection (b)(4), which forbids the imposition of "another tax that discriminates against a rail carrier providing transportation," is not as clear.

Id. at 337 (emphasis added). This Court further recognized with regard to subsections (b)(1)-(3): "In drafting [section 11501], Congress prohibited discriminatory tax rates and assessment ratios *in no uncertain terms*, and set forth *precise standards for judicial scrutiny* of challenged rate and assessment practices." *Id.* at 343 (internal citations omitted) (emphasis added). As explained in *Oklahoma Tax*, one of those "precise standards for judicial scrutiny" is the Subsection (b)(1) formula, which requires proof of the railroad property's "true market value." See 481 U.S. at 461-62.

Congress made a clear choice to outlaw discrimination against railroads in property assessments, and granted railroads a remedy in federal court to enforce that antidiscrimination right. Congress defined a ratio of assessed to "true market value" as the measure of discrimination between railroad property and other commercial and industrial property, and committed the determination of "true market value" to the federal district court. It simply makes no sense to interpret Section 11501(b)(1) to disable railroads from challenging (and federal courts from reviewing) the principal means by which States may accomplish discrimination: by choosing improper methods that inflate estimations of the market value of railroad property.

* * * *

Section 11501 requires courts to determine the "true market value" of railroad property based upon any and all competent evidence. However, the decision of the court below, by forbidding consideration of appropriate "accounting methods," expansively defined as "all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be," Pet. App. 17a, effectively immunizes much discrimination from the federal judicial remedy of Section 11501. Consequently, States have an incentive to adopt discriminatory methods of valuing railroad property. Unless this Court grants this petition and strikes this judicially created "methodology" exception, Congress's intent to eliminate discriminatory taxation of the railroad industry will have been successfully thwarted by the States.

III. IMMEDIATE REVIEW IS NECESSARY BECAUSE THE RULE BELOW HANDCUFFS RAILROADS IN CHALLENGING THE RECENT RAPID AND AGGRESSIVE ESCALATION OF STATE PROPERTY VALUATIONS.

States revalue railroad property for tax assessments on an annual basis. The Eleventh Circuit's bar on valuation chal-

lenges openly invites state tax officials to devise discriminatory methods for valuing railroad property. Indeed, as discussed below, there is already evidence that state appraisers are becoming bolder in their determinations of "true market value" for railroads running through their States. These developments make this Court's immediate intervention all the more necessary.

With state governments under substantial fiscal pressure, it is not surprising that a judicial decision immunizing valuation methodologies from federal court review would spur States to become more aggressive in valuing railroad property, with dire financial consequences for the railroads. The Fourth Circuit's *Chesapeake Western* decision had just such an effect. After the Fourth Circuit issued *Chesapeake Western* on July 12, 1991, the Virginia Department of Taxation certified revised assessments for the 1988 and 1989 tax years on August 23, 1991, barely enough time to let the ink dry on the *Chesapeake Western* opinion. *Forst*, 4 F.3d at 247. The Fourth Circuit recognized that "[t]he revisions produced substantial increases in the assessed values of [the plaintiff-railroad's] property." *Id.* Specifically, the Fourth Circuit highlighted that Virginia had changed its methods when it certified the revised assessments and that under the revised method, the plaintiff-railroad's assessment for tax year 1988 in Alexandria increased from $15,293,168 to $111,663,882—an increase of 730 percent over the original assessment. *Id.*

Similarly, in the wake of the district court decision in this case, Georgia has substantially increased its estimation of the unit value of CSXT and other railroads. As noted above, the 2002 Georgia taxable value for CSXT was $514.9 million, 36.3% higher than the 2001 value. See *supra*, at 7. In 2006, the Georgia appraiser used a new appraisal method, which resulted in an average Georgia taxable value increase of 46.6% for properties of all railroads operating in the State. See State Bd. of Equalization, *Public Utility and Airline Flight Equipment Digest* 2 (2006). By contrast, the average

Georgia taxable value for all other centrally assessed properties increased by only 5.6%. See *id.* For CSXT, Georgia's new appraisal method resulted in a unit value of $11.2 billion, and consequently a Georgia taxable value of $762 million. That was a 40.6% increase over the 2005 Georgia taxable value. If the Eleventh Circuit's decision stands, railroads will be handcuffed in remedying such discrimination, because of these limitations placed on challenges to the values as fixed by the States.

Nor are the recent jumps in estimated unit value isolated occurrences limited to Georgia. For the 2003 tax year, Florida initially valued CSXT at $13 billion, which resulted in a Florida taxable value of about $723 million. CSXT brought suit in federal court to challenge that overvaluation, and the parties subsequently settled at a Florida taxable value of $488 million. The $488 million settlement was part of a three-year settlement, in which the CSXT taxable value in Florida dropped to $478 million for 2004 and to $468 million for 2005. The settlement was executed before the district court issued its decision below in this case. Subsequently, when the settlement expired in 2006, Florida valued CSXT at approximately $12.9 billion, which was a 57% increase over the unit value found by the district court below. The new unit value resulted in a Florida taxable value in 2006 that was 49% higher than the 2005 settlement value. CSXT's property tax in Florida rose from $8.7 million in 2005 to $13.2 million in 2006, an increase of 52%. Yet CSXT may be impermissibly precluded by the decision below from challenging in federal court anything but the state appraiser's "factual determinations."

The portrait in the States where CSXT operates is not only one of rapid and unjustifiable inflation of railroad property valuations, but also increasing arbitrariness. CSXT's national unit value in a given year is, in theory, a single number. In practice, however, each year some States adopt breathtakingly high unit values that far exceed the range of values adopted

by most States. In the 2006 tax year, for example, Georgia and Florida had adopted CSXT unit values of $11.2 and $12.9 billion respectively, which far exceeded the average value of $7.1 billion in the other States in the Fourth and Eleventh Circuits that use the unit value method. Such prejudicial and arbitrary variation in valuations of railroad property could be remedied if the 4-R Act were given its intended scope, and if federal district courts were given proper latitude to determine the "true market value" of railroad property, rather than deferring to the self-interested valuation methods employed by state tax agencies.

In the face of the aggressive and discriminatory escalation of railroad property valuations and tax burdens, this Court should not leave unsettled the important question of the scope of the federal antidiscrimination remedy of Section 11501(b)(1) of the 4-R Act on which the lower courts are divided. The amount of taxes that are now being discriminatorily assessed on railroad property far exceed the $50 million in overtaxation that prompted Congress to pass the 4-R Act in the 1970's. H.R. Rep. No. 94-725, at 78. Discrimination in property tax assessments is particularly insidious because state taxable values tend inexorably to increase over time. Discriminatory assessments for tax years that are currently in litigation or settlement negotiations will be forever lost to railroads if this Court were to defer review. Intervention by this Court is imperative to resolve the circuit conflict, and to rectify the state methodology abuses that are currently practiced.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Ave., NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON,
BEARMAN, CALDWELL
& BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

* Counsel of Record

March 23, 2007

APPENDIX

APPENDIX A

UNITED STATES COURT OF APPEALS
ELEVENTH CIRCUIT

No. 05-16000

CSX TRANSPORTATION, INC.,
Plaintiff-Appellant,

v.

STATE BOARD OF EQUALIZATION, of the State of Georgia, JERRY JACKSON, as Commissioner of Revenue of the State of Georgia, RUSSELL W. HINTON, as State Auditor of the State of Georgia, RAY J. CRAWFORD, as Director of the Georgia State Properties Commission,
Defendants-Appellees.

Dec. 19, 2006

Appeal from the United States District Court
for the Northern District of Georgia.

Before BIRCH, PRYOR and FAY, *Circuit Judges.*

PRYOR, *Circuit Judge*:

This appeal presents a question about state taxation of railroad properties that was expressly left open by the Supreme Court of the United States, has since divided the federal appellate courts, and involves the traditional balance of federal and state power. We are asked to decide whether section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 (4-R Act or the Act), 49 U.S.C. § 11501, allows a railroad to challenge the methodology by which a state determines the true market value of railroad property for

ad valorem tax purposes. The 4-R Act provides an exception to the general rule of the Tax Injunction Act that federal district courts will not interfere with matters of state taxation. *Compare id. with* 28 U.S.C. § 1341. This appeal turns on the breadth of that exception.

CSX Transportation, Inc. (the Railroad) filed a complaint against the State Board of Equalization of Georgia (the Board), under section 306 of the Act, in which it challenged the appraisal of its property by the Board at $8.2 billion. Section 306 requires, for purposes of levying a property tax, that the ratio of assessed value to true market value of railroad property not exceed by more than five percent the ratio of assessed value to true market value of all other commercial and industrial property in the same assessment jurisdiction. 49 U.S.C. § 11501(c). The district court refused to consider an appraisal proffered by the Railroad that valued the property of the Railroad at $6 billion because the district court concluded that the appraisal was based on a valuation methodology different from the one used by the State. *CSX Transp. v. State Bd. of Equalization*, 448 F.Supp.2d 1330, 1348 (N.D.Ga.2005). The Railroad argues that the 4-R Act allows it to challenge the valuation methodology of a state. Because the Act does not clearly state that railroads may challenge state valuation methodologies, we affirm the judgment of the district court.

I. BACKGROUND

The Railroad is a wholly-owned subsidiary of CSX Corporation. In tax year 2002, the Railroad provided freight transportation over a network that included a route through the State of Georgia. In Georgia, public utilities are centrally-assessed taxpayers, and public utilities include railroads, investor-owned electric utilities, investor-owned telephone companies, pipeline companies, and gas distribution companies. Although most taxpayers in Georgia are assessed, in the first instance, by county boards of assessors, the State

Revenue Commissioner issues proposed assessments of the property of centrally-assessed taxpayers for each county in which the taxpayer owns taxable property. The Property Tax Division of the Georgia Department of Revenue (the Department) prepares a digest of public utility assessments that the Board reviews and approves. The Board then certifies the proposed assessments to each county in which taxable property is owned. Ga.Code Ann. § 48-2-18(c). Each county "may, but is not required to, use these figures as the county's own tax assessment." *Colonial Pipeline Co. v. Collins*, 921 F.2d 1237, 1240-41 (11th Cir.1991). For 2002, 59 of the 71 Georgia counties in which the Railroad owned taxable property adopted the proposed assessment of the Board.

In 2002, as in preceding years, the Department determined the value of all public utilities using the unit rule. Under this rule, an appraiser first determines the value of all assets of an entity, regardless of location. That amount is then multiplied by the percentage of the entity located within Georgia to determine what portion of the value of the company should be allocated to the state. The Railroad agrees that the unit rule is a proper method of valuation under Georgia law.

Although there are several different methods for determining the value of a company or property under the unit rule, those methods fall into three general categories: the sales comparison approach, the cost approach, and the income approach. Under a sales comparison approach, a company or property is appraised by examining actual sales of comparable companies or properties. Under the cost approach, an appraiser adds together the original costs of the various components of a company or property and makes deductions for depreciation or obsolescence. Under an income approach, an appraiser determines the future income stream of a company or property over the life of the company or property.

Gregg Dickerson prepared the valuation worksheets for the appraisal of the Railroad in 2002. Dickerson was an ap-

praiser with 30 years of experience, including experience regarding the use of the unit rule in public utility valuation. Dickerson performed unit valuations at the Department for ten years before leaving in 1993 to work in the tax department at Norfolk Southern Railroad. Dickerson returned to the Department in 2001 to serve as the Program Manager of its Public Utilities section.

When Dickerson returned to the Department, he altered the combination of valuation methods the Department used to calculate value under the unit rule. The Department had been calculating the unit values of all public utilities using a yield capitalization method (an income approach), a direct capitalization method (another income approach), and a stock and debt method (a sales comparison approach). For tax year 2002, Dickerson replaced the first two methods with a discounted cash flow method (an income approach) and a market multiples method (a sales comparison approach). Dickerson retained the third method.

Dickerson appraised the property of the Railroad using these three methods. He first used the stock and debt method, which assumes that the value of a company equals the sum of its outstanding debt and its equity. Under this method, Dickerson's appraisal was $12.022 billion.

Dickerson next used the discounted cash flow method. Under this method, an appraiser first projects the cash flows of a company for a designated number of years after the assessment date and discounts those expected cash flows to their present value. The appraiser then calculates a terminal or reversion value that represents the value of the company at the end of the projection period. These two values together give the appraiser his unit value for the company. Dickerson calculated four terminal values using different indicators of reversion. The unit value calculated using a terminal growth rate of 63 percent was the lowest of the four, and Dickerson

selected that value. Dickerson's appraisal, under this method, was $8,126,293,350.

Finally, Dickerson used the market multiples method. This method requires an appraiser to derive market multiples from the stock prices of companies engaged in similar lines of business and compare those multiples with the subject company to determine its value. Dickerson performed three different market multiples analyses, which resulted in appraisals of $12.346 billion, $10.769 billion, and $8.474 billion.

The five values derived from these three methods gave Dickerson a valuation range of $8.126 to $12.346 billion. As he did with all public utilities that year, Dickerson selected an amount at the lower end of that range to avoid potential litigation. Dickerson selected $8.2 billion as the lower limit of what the unit value of the Railroad might reasonably be. He then deducted $400 million to account for intangible property not subject to *ad valorem* taxation. Ga.Code Ann. § 48-6-21. The adjusted unit value of $7.8 billion was multiplied by 7.194059 percent, which was the percentage of the track of the Railroad located in Georgia, which resulted in an allocated value of $561,136,602. Dickerson made further deductions for motor vehicles, pollution control equipment, and an exempt rail line, and he arrived at a taxable fair market value of $514,862,672.

The Railroad filed a complaint under the 4-R Act that challenged the valuation proposed by the Department. The Act bars states from discriminating against railroads when levying property taxes:

> The following acts unreasonably burden and discriminate against interstate commerce, and a State, subdivision of a State, or authority acting for a State or subdivision of a State may not do any of them:
>
> (1) Assess rail transportation property at a value that has a higher ratio to the true market value of the rail

> transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
>
> (2) Levy or collect a tax on an assessment that may not be made under paragraph (1) of this subsection.
>
> (3) Levy or collect an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.
>
> (4) Impose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the Board under this part.

49 U.S.C. § 11501(b).

When a violation of the 4-R Act reaches a certain quantitative threshold, redress is allowed as an exception to the Tax Injunction Act, 28 U.S.C. § 341, which ordinarily bars challenges of state taxation practices in federal courts:

> Notwithstanding section 1341 of title 28 and without regard to the amount in controversy or citizenship of the parties, a district court of the United States has jurisdiction, concurrent with other jurisdiction of courts of the United States and the States, to prevent a violation of subsection (b) of this section. Relief may be granted under this subsection only if the ratio of assessed value to true market value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction. The burden of proof in determining assessed value and true market value is governed by State law.

49 U.S.C. § 11501(c).

The Railroad argued that it was taxed at a higher ratio of assessed value to true market value than other commercial and industrial property, in violation of section 11501(b)(1), because the true market value of its property for 2002 did not exceed $6 billion. The Railroad submitted an appraisal prepared by Thomas Tegarden, whose credentials the district court described as "impeccable." *CSX Transp.*, 448 F.Supp.2d at 1333. Tegarden used three valuation methods, two of which had not been used by the Department: a stock and debt method, a cost method, and a yield capitalization method. These methods produced valuations of $9.367 billion, $6.15 billion, and $5.983 billion, respectively. Tegarden gave no weight to his stock and debt value, little weight to his cost value, and primary weight to his yield capitalization value, and concluded that the unit value of the Railroad for tax year 2002 did not exceed $6 billion. Tegarden made the same adjustments as the Department for intangible property, motor vehicles, pollution control equipment, and the exempt rail line, and applied the same track-mile percentage, which resulted in a taxable fair market value of not more than $369,253,752.

The district court concluded that it was not permitted to consider Tegarden's appraisal. The district court interpreted the 4-R Act to bar consideration of appraisals based on a valuation methodology different from the methodology used by the State, unless the methodology of the State is irrational or intentionally discriminatory. *Id.* at 1342. The court rejected the argument that Tegarden's valuation methodology was a variant of the same methodology used by the State. *Id.* at 1343.

The Railroad also challenged the accuracy of several calculations by the Department in its appraisal. In one of these challenges, the Railroad argued that the Department erred in using 6.3 percent as the terminal growth rate in its discounted cash flow valuation. The terminal growth rate

plays a central role in determining the terminal or reversion value in the discounted cash flow method of valuation. Dickerson testified that he chose this rate because it is the long-term growth rate of the gross domestic product and is the type of rate the market would use to estimate the terminal value of a company using a discounted cash flow method. The Railroad argued that this rate was higher than the growth rate used to project cash flows through 2011 (the first half of the discounted cash flow valuation) and, because the Department projected that the revenue of the Railroad would grow at only 2 percent, a growth rate of 6.3 percent would require that expenses become negative.

The district court found that the testimony of the experts of the Railroad on this issue lacked credibility. *Id.* at 1345. The court also found that these experts never stated what the growth rate should actually be. At most, their testimony suggested the Department should have used a rate of 3.5 percent or 4.5 percent, but the court concluded that these rates suffered from the same infirmities as the 6.3 percent rate, including that they would require expenses to become negative. *Id.*

After rejecting the arguments of the Railroad, the district court concluded that the true market value of the Railroad for tax year 2002 was $7,726,293,350. *Id.* at 1350. The court found the figure produced by the discounted cash flow method to be the most accurate appraisal of the value of the Railroad, and the court subtracted $400 million from the discounted cash flow value of the Department ($8,126,293,350) to account for intangible property. *Id.* at 1350 n. 23. The court concluded that the ratio of assessed value to true market value of the property of the Railroad did not exceed by more than five percent the ratio of assessed value to true market value of the other commercial and industrial property in the assessment jurisdiction of the Railroad. *Id.* at 1350. The district court entered a judgment in favor of the Board.

II. STANDARDS OF REVIEW

We review factual findings of the district court for clear error and conclusions of law *de novo*. *Glassroth v. Moore*, 335 F.3d 1282, 1296-97 (11th Cir.2003).

III. DISCUSSION

The Railroad raises three challenges to the determination by the district court of its true market value for tax year 2002. The Railroad first contends that the district court erred in holding that the 4-R Act bars a railroad from challenging the valuation methodology chosen by a state. Second, the Railroad argues that, even if it is barred from challenging the methodology of the Board, the appraisal of Tegarden should have been considered by the district court because that appraisal was based on the same methodology used by the Board. Third, the Railroad maintains that the district court clearly erred in accepting the use by the Board of a terminal growth rate of 6.3 percent in its discounted cash flow valuation. We address each argument in turn.

A. The 4-R Act Does Not Allow a Railroad to Challenge the Methodology by Which a State Determines Fair Market Value.

Whether a railroad may challenge, under the 4-R Act, the valuation methodology of a state is a question the Supreme Court has acknowledged but not decided. When it first interpreted the 4-R Act in *Burlington Northern Railroad v. Oklahoma Tax Commission*, the Court held that a railroad need not prove intentional discrimination to challenge factual determinations made by a state in the application of its valuation methodology. 481 U.S. 454, 462-63, 107 S.Ct. 1855, 1860-61, 95 L.Ed.2d 404 (1987). In a footnote, the Court expressly refrained from deciding whether the Act allows a railroad to challenge the valuation methodology itself:

> This case therefore does not present the question whether a railroad may, in an action under § 11503 [now

> § 11501], challenge in the district court the appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied. Accordingly we express no view on that issue.

Id. at 463 n. 5, 107 S.Ct. at 1861 n. 5.

Three of our sister circuits, following *Burlington Northern v. Oklahoma*, have split on whether railroads may challenge state valuation methodologies. The Fourth Circuit, on the one hand, has concluded that the 4-R Act does not permit a railroad to challenge the valuation methodology of a state. That circuit concluded that the text of the Act is ambiguous, and the court was "not inclined to disregard" the general policy of noninterference in matters of state taxation contained in the Tax Injunction Act "where § 306 does not plainly authorize such an exception." *Chesapeake W. Ry. v. Forst*, 938 F.2d 528, 531 (4th Cir.1991); *accord Richmond, Fredericksburg & Potomac R.R. Co. v. Forst*, 4 F.3d 244, 250 (4th Cir.1993). The Second and Ninth Circuits, on the other hand, have repudiated *Chesapeake Western* and held that railroads may challenge valuation methodologies. In *Burlington Northern Railroad v. Department of Revenue*, the Ninth Circuit explained that section 11501(c) of the 4-R Act provides that state law governs the burden of proof in challenges to assessed value and true market value. 23 F.3d 239, 241 (9th Cir.1994). Because determinations of property value by public officials in the State of Washington may be defeated by "clear, cogent and convincing evidence," the court reasoned that state valuation methodologies may likewise be defeated by clear, cogent, and convincing evidence. *Id.* In *Consolidated Rail Corp. v. Town of Hyde Park*, the Second Circuit held that, at least where states use a unique method to appraise railroads, the 4-R Act allows railroads to challenge valuation methodology. 47 F.3d 473, 482 (2d Cir.1995).

The Railroad argues that *Chesapeake Western* was wrongly decided and urges us to follow *Burlington Northern v. Department of Revenue* and *Consolidated Rail* in allowing railroads to challenge valuation methodology. The Railroad contends that the 4-R Act allows a challenge of any act, including the choice of a methodology, that has the effect of discriminating against railroads. The Railroad relies on the statement of the Court in *Burlington Northern v. Oklahoma* that the Act "speaks only in terms of 'acts' which 'unreasonably burden and discriminate against interstate commerce'; nowhere does it refer to the intent of the actor." 481 U.S. at 463, 107 S.Ct. at 1861.

The Railroad also relies on broad statements in previous decisions of our Court. The Railroad reminds us that we have stated that "[t]he legislative history and broad language of the Act show Congress possessed a general concern with discrimination in all of its guises." *S. Ry. v. State Bd. of Equalization*, 715 F.2d 522, 528 (11th Cir.1983). We also have stated that "Congress meant unconditionally to ensure a federal forum for section 11503 [now section 11501] claims." *Id.* at 527.

Notwithstanding our earlier dicta to the contrary, we are persuaded that the Fourth Circuit correctly interpreted the 4-R Act as being subject to a clear statement rule. It is a well-settled principle of statutory interpretation that a statute will not be construed to burden states in the exercise of their traditional powers unless it clearly states its intent to do so. "'If Congress intends to alter the usual constitutional balance between the States and the Federal Government, it must make its intention to do so unmistakably clear in the language of the statute.'" *Gregory v. Ashcroft*, 501 U.S. 452, 460-61, 111 S.Ct. 2395, 2401, 115 L.Ed.2d 410 (1991) (quoting *Atascadero State Hosp. v. Scanlon*, 473 U.S. 234, 242, 105 S.Ct. 3142, 3147, 87 L.Ed.2d 171 (1985)). "This plain statement rule is nothing more than an acknowledgment that the States

retain substantial sovereign powers under our constitutional scheme, powers with which Congress does not readily interfere." *Id.* at 461, 111 S.Ct. at 2401.

Perhaps the most fundamental power of a sovereign is the power to tax. This power was originally considered so integral a power of the states as to admit of no abridgement by the federal government, *see* The Federalist No. 32 (Alexander Hamilton), and its singular importance to the states has been repeatedly acknowledged. *See Dep't of Revenue v. ACF Indus.*, 510 U.S. 332, 345, 114 S.Ct. 843, 850, 127 L.Ed.2d 165 (1994) (power to tax is "central to state sovereignty"); *Bode v. Barrett*, 344 U.S. 583, 585, 73 S.Ct. 468, 470, 97 L.Ed. 567 (1953) (power of a state to tax is "basic to its sovereignty"); *Curry v. McCanless*, 307 U.S. 357, 366, 59 S.Ct. 900, 905, 83 L.Ed. 1339 (1939) (power to tax is "incident to" and "coextensive with" sovereignty). This understanding of the relationship of sovereignty and taxation is implicit: "It is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments." *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110, 20 L.Ed. 65 (1871).

The selection of a valuation methodology is part of this fundamental power of a state. *See Louisville & Nashville R.R. v. Dep't of Revenue, Fla.*, 736 F.2d 1495, 1498 (11th Cir.1984) ("These arguments broach delicate issues implicating the state's traditional authority to select methods of valuation."). Important questions of state policy are often intertwined with the selection of a valuation methodology. Time pressures and limited resources, for example, may compel a state to choose a simple valuation methodology rather than a complicated one. *See, e.g., Union Pac. R.R. v. State Tax Comm'n*, 716 F.Supp. 543, 557 (D.Utah 1988).

The Supreme Court has "long recognized that principles of federalism and comity generally counsel that courts should adopt a hands-off approach with respect to state tax admin-

istration." *Nat'l Private Truck Council v. Okla. Tax Comm'n*, 515 U.S. 582, 586, 115 S.Ct. 2351, 2354, 132 L.Ed.2d 509 (1995). Because the states rely so heavily on their ability to tax, "'it is of the utmost importance to all of them that the modes adopted to enforce the taxes levied should be interfered with as little as possible.'" *Id.* (quoting *Dows*, 78 U.S. (11 Wall.) at 110). When Congress enacted the Tax Injunction Act, it "intended to codify this pre-existing federal equity practice and to ensure more uniform adherence to the underlying principles of comity." *S. Ry.*, 715 F.2d at 527; *see also 28 E. Jackson Enters. v. Cullerton*, 523 F.2d 439, 441 (7th Cir.1975) (Tax Injunction Act "codifies the well-established federal policy of noninterference in matters of state taxation").

The Railroad argues that principles of federalism and comity should play no role in our interpretation of the 4-R Act. This argument is not new. We have stated that "Congress intended to carve out an exception not only to the Tax Injunction Act, but also to the underlying doctrine of equitable restraint in the narrow area of discriminatory taxation of railroads," *S. Ry.*, 715 F.2d at 529, and the Eighth Circuit has stated that "[t]he common law principle of federal deference to state tax schemes, as amplified by 28 U.S.C. § 1341, has no place in a § 306 analysis," *Burlington N. R.R. v. James*, 911 F.2d 1297, 1300 (8th Cir.1990).

The problem with this argument is that more recently the Supreme Court has stated the opposite. In a decision mentioned by neither the Ninth Circuit in *Burlington Northern v. Department of Revenue* nor the Second Circuit in *Consolidated Rail*, the Supreme Court ruled in 1994 that states may grant exemptions from a generally applicable *ad valorem* property tax without subjecting the taxation of railroad property to challenge under subsection (b)(4) of the Act. *ACF Indus.*, 510 U.S. at 335, 114 S.Ct. at 846. The Court reached this conclusion based on the text of the Act, *id.* at

339-43, 114 S.Ct. at 848-50, and then explained, "Principles of federalism support, in fact compel, our view. Subsection (b)(4), *like the whole of § 11503* [now § 11501], sets limits upon the taxation authority of state government, an authority we have recognized as central to state sovereignty," *id.* at 345, 114 S.Ct. at 850 (emphasis added). The Court stated that principles of federalism required the use of a clear statement rule in this context. *Id.* at 345, 114 S.Ct. at 850-51. Because it was not the "clear and manifest purpose of Congress" to allow railroads to challenge property tax exemptions in federal court, the Court refused to read the 4-R Act as granting them that right. *Id.*

Based on the reasoning of the Court in *ACF Industries*, we conclude that railroads may not challenge state valuation methodologies under subsection (b)(1). The text of the Act does not clearly state that railroads may challenge valuation methodologies. Without that clear statement of congressional intent, the argument of the Railroad fails.

The legislative history, "to the extent it has any relevance to our inquiry," *ACF Indus.*, 510 U.S. at 345, 114 S.Ct. at 851, supports the conclusion that railroads may not challenge state valuation methodologies in federal court. The committee report regarding a precursor of section 306 explained that the bill "does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves. It merely provides a single standard against which all affected assessments must be measured." S.Rep. No. 90-1483, app. B, at 22 (1968). The testimony of a railroad representative at a hearing on an earlier version of section 306 was consistent with this interpretation: "The standards and methods of valuation that any State wishes to use would be unaffected by this legislation." *Hearing on H.R. 16245 Before the Subcomm. on Transp. & Aeronautics of the H. Comm. on Interstate & Foreign Commerce*, 91st Cong. 138 (1970) (statement of Philip M. Lanier).

The most that can be said for the argument of the Railroad is that it was articulated ably in the dissenting opinion in *ACF Industries*. Justice Stevens argued that "the text of subsection (b)(4) and its evident purposes convince me that Congress intended to bar discrimination by any means, including exemptions." *ACF Indus.*, 510 U.S. at 350, 114 S.Ct. at 853 (Stevens, J., dissenting). The lower court that the Supreme Court in *ACF Industries* reversed also reached this conclusion. *See id.* at 338, 114 S.Ct. at 847 ("The court [of appeals] explained that Congress enacted § 11503 [now § 11501] to 'prevent tax discrimination against railroads *in any form whatsoever.*'" (citation omitted)). We obviously are not at liberty to follow either Justice Stevens's dissenting opinion or the decision reversed by the Supreme Court. The district court was not allowed to consider a valuation methodology different from the methodology of the Board.

B. The District Court Did Not Clearly Err in Finding That the Railroad Used a Valuation Methodology Different From the Methodology of the State.

The Railroad and an amicus curiae argue, in the alternative, that the appraisal by Tegarden was based on the same methodology used by the State. The American Association of Railroads, as amicus curiae, argues that there is a tri-partite taxonomy of appraisal terminology consisting in unit rule and summation "methodologies"; income, cost, and market "approaches" for determining value under the unit rule; and stock and debt, discounted cash flow, yield capitalization, and other "techniques" for implementing the various approaches. Under this taxonomy, our decision in subsection III.A would bar the Railroad from challenging only the adoption of the unit rule.

Although this taxonomy may be useful within the appraisal community, there is little legal support for this argument. The Association argues that the Fourth Circuit has used the terms "method" and "methodology" in the way it advocates,

. *see Chesapeake W. Ry.*, 938 F.2d at 529, but other courts have used those terms to designate more specific components of the valuation process. *See, e.g., Consol. Rail*, 47 F.3d at 477 (discussing "the 'income capitalization method'" and "the 'stock and debt method'"); *Union Pac. R.R.*, 716 F.Supp. at 551 (referring to "yield capitalization" and "direct capitalization" as different methods and methodologies).

The more serious problem for the Association is that its argument is contrary to the understanding of the Supreme Court. A close reading of footnote 5 of *Burlington Northern v. Oklahoma* establishes that the Supreme Court understands the phrase "accounting methods" to encompass all nonfactual determinations made in the process of appraising a railroad. We quote the text of that footnote as follows, with our emphasis on three key phrases:

> This case therefore does not present the question whether a railroad may, in an action under § 11503 [now § 11501], challenge in the district court the appropriateness of the *accounting methods* by which the State determined the railroad's value, *or is instead restricted* to challenging the *factual determinations* to which the State's preferred accounting methods were applied. Accordingly we express no view on that issue.

481 U.S. at 463 n. 5, 107 S.Ct. at 1861 n. 5 (emphasis added).

This language suggests that there are only two categories in the valuation process, and the Court understood "accounting methods" and "factual determinations" to be exhaustive of all possibilities. It would not make sense to say that railroads, if barred from challenging accounting methods, would be "instead restricted" to challenging factual determinations if there were some third category in the valuation process, such as an "approach" or "technique," as the Association argues. The inability of railroads to challenge accounting methods restricts the railroads to challenging factual determinations.

The term "accounting methods" and the parallel term "valuation methodology" as used by the Supreme Court encompass all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be.

The definition of a "methodology" also should be understood in the light of the principles of federalism that govern our interpretation of the 4-R Act. Under the taxonomy advanced by the Association, a railroad would be barred from challenging the decision to use the unit rule, but permitted to challenge the use of a combination of the stock and debt method and a market multiples approach instead of a yield capitalization method and a cost approach. We are reluctant to allow that kind of freewheeling judicial second-guessing, which implicates delicate matters of state policy, *cf. Union Pac. R.R.*, 716 F.Supp. at 557 (explaining what might influence a choice between a direct capitalization and a yield capitalization method), without clear support in the text of the Act. We would expect Congress to state unambiguously its intention to subject states to challenges of both kinds of decisions in federal court.

Based on our understanding of the term "methodology," the district court did not clearly err in finding that the appraisal prepared for the Railroad by Tegarden was based on a methodology different from the methodology used by the State. The State appraised public utilities in 2002 by calculating five values under three different methods and selecting a figure at the low end of the resulting range. Tegarden calculated three values using three methods, only one of which had been used by the State. Instead of selecting a figure at the low end of his resulting range, Tegarden weighted each result, giving primary weight to one of the methods—yield capitalization—not used by the State. Even if the Railroad were able to convince us that the yield capitalization and discounted cash flow methods are alge-

braically the same, this conclusion would not establish that Tegarden used the same valuation methodology as the State. The State did not give primary weight—or any weight—to its discounted cash flow valuation. The selection by the Department of an appraisal amount nearest to the discounted cash flow number did not reflect the conclusion that discounted cash flow was the most accurate of the methods used, only that it was the lowest.

C. The District Court Did Not Clearly Err When It Accepted the 6.3 Percent Terminal Growth Rate Used by the State.

Finally, there was no clear error by the district court in its finding that the use of a terminal growth rate of 6.3 percent by the Board, in its discounted cash flow valuation, was acceptable. A factual finding "is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-74, 105 S.Ct. 1504, 1511, 84 L.Ed.2d 518 (1985) (internal quotations and citations omitted). We cannot say definitively that the district court made a mistake because its finding rested on issues of expert credibility.

Although the experts employed by the Railroad testified that a terminal growth rate of 6.3 percent was too high, Dickerson explained why he found it to be appropriate, including that 6.3 percent is the long-term growth rate of the gross domestic product. The district court stated that it found the experts of the Railroad to lack credibility on this issue. *CSX Transp.*, 448 F.Supp.2d at 1345. We have previously said that we "should be reluctant to overturn the district court's findings" where those findings are based on "crucial evaluations of witness credibility, particularly where the expert testimony conflicted." *L&C Marine Transp., Ltd. v. Ward*, 755 F.2d 1457, 1461 (11th Cir.1985).

The district court also based its finding on the failure of the Railroad to state what the terminal growth rate should be. *CSX Transp.*, 448 F.Supp.2d at 1345. At most, the testimony of its experts suggested that the Department should have adopted 3.5 percent or 4.5 percent as the terminal growth rate. *Id.* Even then, as the district court found, these rates suffered from the same alleged infirmities as the rate of 6.3 percent chosen by Dickerson, including that the rates would require expenses to become negative. *Id.* Based on this record, the district court did not clearly err.

IV. CONCLUSION

The judgment of the district court is

AFFIRMED.

FAY, *Circuit Judge*, concurring in part and dissenting in part:

As set forth in the majority opinion, the Railroad raises three issues in this appeal. The majority rejects all three of the Railroad's contentions. I agree that issues two and three have no merit. The district court did not err in finding Tegarden's appraisal was not based upon the same methodology as that used by the Board nor in accepting the 6.3 percent terminal growth rate used by the Board in its discounted cash flow evaluation.

Most respectfully, however, I disagree with the majority's holding that the 4-R Act bars the Railroad from challenging the valuation methodology chosen by the state. As acknowledged by the majority, our sister circuits have split on this issue. This gives me a little concern because in my opinion there is nothing ambiguous or complicated about these statutes.

Congress passed the Tax Injunction Act, 28 U.S.C. § 1341, which federal courts have enforced with great zeal. Congress, just as clearly, enacted the Railroad Revitalization and Regulatory Reform Act of 1976 (4-R Act), 49 U.S.C. § 11501, to correct a perceived evil; to wit: discriminatory tax practices by the states upon our national rail transportation system. The 4-R Act is a specific exception and excluded from the provisions of the Tax Injunction Act. 49 U.S.C. § 11501(c).

The language of the statute is straightforward and prohibits states from assessing rail transportation property at a value that has a higher ratio to the true market value than the ratio that the assessed value of other commercial and industrial property has to its true market value. If such a variation exists and exceeds five percent, relief may be granted to the railroad.

The only reference dealing with how such may be shown is a sentence that specifies that "the burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. § 11501(c). It is apparent from the record in this case that there are many methodologies that can be used in assessing the value of property. No one has suggested that Georgia law approves of some and disapproves of others.[1] Surely a state could not use one method to assess

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[1] A quick glance at some Georgia cases shows that the method of appraising value is often in dispute. See *Rogers v. De Kalb County Bd. of Tax Assessors*, 247 Ga. 726, 279 S.E.2d 223 (Ga.1981), where the plaintiff sought an injunction prohibiting the Board of Tax Assessors from using the published market (i.e., "blue book") value to assess his aircraft and requiring them to value and assess the aircraft on the basis of original cost minus depreciation, the method more commonly employed to value business equipment, furniture and fixtures. The plaintiff argued that aircraft represented tangible property just as business equipment, furniture and fixtures did, and that Georgia law required uniform taxation of property within the same class. The Georgia Supreme Court held that: "it is not '[im]permissible under the uniformity of taxation provision of the constitution to apply different methods of arriving at the fair market value of tangible property.'" *Id.* at 728, 279 S.E.2d 223, (citing *Wade v. Ray*, 234 Ga. 234 (214 S.E.2d 923) (1975)). See also *Chilivis v. Backus*, 236 Ga. 88, 90 (222 S.E.2d 371) (1976), where the Supreme Court of Georgia reviewed a lower court ruling that prohibited the county tax assessor from considering any factor other than actual use in arriving at fair market value. Holding that actual use is a determinative, but not exclusive, factor for determining a property's fair market value, the Court observed that: "[t]he object of the assessors must be to determine the fair market value of the property subject to taxation in the county and the methods employed may be varied if the object is attained." See also *Colvard v. Ridley*, 218 Ga. 490, 128 S.E.2d 732 (1962), where the taxpayer alleged that the tax assessors had taxed their real and personal property according to different methods, violating the state mandate for uniform taxation within a given class of property. The Supreme Court of Georgia held that: "[w]hile tax assessors were permitted a wide range of tools of placing a value on property, they were required to use the same valuation tool when placing a value on property within one class." *Id.* at 491, 128 S.E.2d 732. Finally, see *Inland Container Corp. v. Paulding County Bd. of Tax Assessors*, 220 Ga.App. 878, 470 S.E.2d 702 (Ga.Ct.App.1996), where two corporate

the market value of railroad property and a different method to assess other commercial and industrial property if such resulted in gross discrimination toward the railroad.

As articulated by the Second Circuit, such a situation would be in direct conflict with the clear meaning of the statute:

> 4. Method of Appraisal
>
> Relying primarily on a decision by the fourth circuit in *Chesapeake Western Ry. v. Forst*, 938 F.2d 528 (4th Cir.1991), the SBEA contends that Conrail is bound by the method of appraisal that the SBEA has chosen, and that since it chose to use the cost approach, it is improper to consider any other method of valuation in fixing the "true market value" of Conrail's properties. The *Chesapeake* court viewed the method of appraisal as a matter of state policy that was beyond the reach of the 4-R Act. We do not accept that interpretation of the statute. What the 4-R Act prohibits is discrimination against railroads in the ratios of two sets of numbers: assessed values and true market values of the railroad's property vis a vis those of other commercial and industrial properties. To avoid the prohibited discrimination, the SBEA must apply the same valuation standards and methods to the railroad property as are used on the commercial and industrial properties to which it is compared. If the Act were to be interpreted, as defendants would have it, so that the SBEA could adopt a special appraisal method for railroads alone, then

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landowners challenged their property tax assessments, arguing that the assessors should have considered "existing use" of the property. Noting that it could only judge the sufficiency of the evidence, not its weight, the Georgia Court of Appeals cautioned, "[n]or may we accept or reject any opposing methods of appraisal presented at trial." *Id.* at 881, 470 S.E.2d 702.

> the whole nondiscrimination objective of the statute could be circumvented.

Consolidated Rail Corp. v. Town of Hyde Park, 47 F.3d 473, 481-82 (2nd Cir.1995).

Since the objective of any methodology is a determination of *true market value,* a railroad should be allowed to challenge the method used in an attempt to prove that the result of such a method was not the *true market value* of its property. In sum, I agree with Justice Stevens that "the text of (the statute) . . . and its evident purposes convince me that Congress intended to bar discrimination by any means . . ." *ACF Industries*, 510 U.S. at 350, 114 S.Ct. at 853 (Stevens, J., dissenting). If the Railroad can prove that the method used by the state does not result in a fair appraisal of true market value and that the assessed value is in fact at a ratio higher than five percent of the ratio of true market value and assessed value of other commercial and industrial property, it is entitled to relief.

Having said all of this, I have no idea whether in this case the Railroad can meet its burden of proof. Although the district court found the Railroad's expert well qualified, other comments raise serious concerns about the weight that would have been given to the opinions expressed. I simply disagree with the absolute preclusion of any challenge to the methodology used by the state in arriving at the true market value of the Railroad's property.

APPENDIX B

UNITED STATES DISTRICT COURT
N.D. GEORGIA
ATLANTA DIVISION

Civil Action No. 1:02-CV-2634-CAP

CSX TRANSPORTATION, INC.,
Plaintiff,

v.

The STATE BOARD OF EQUALIZATION of the State of Georgia; BART L. GRAHAM, Commissioner of Revenue of the State of Georgia; RUSSELL W. HINTON, State Auditor of the State of Georgia; and RAY J. CRAWFORD, Director of the Georgia State Properties Commission,
Defendants.

Sept. 29, 2005

ORDER

PANNELL, *District Judge*.

The plaintiff, CSX Transportation, Inc. ("CSXT") filed this suit under Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976, Pub.L. 94-210, 90 Stat. 54 (Feb. 5, 1976), which is now codified at 49 U.S.C. § 11501 (the "4-R Act"). The 4-R Act confers concurrent jurisdiction on federal district courts to enforce its provisions, so long as "the ratio of assessed value to true market value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." *Id.* § 11501(c). Such jurisdiction lies notwithstanding the Tax Injunction Act of 1937, 28 U.S.C. § 1341, which ordinarily

prohibits district courts from enjoining, suspending or restraining the assessment, levy or collection of taxes under state law where the party may have a plain, speedy, and efficient remedy in state court. *Id.; Southern Railway Co. v. State Board of Equalization*, 715 F.2d 522, 526 (11th Cir.1983).

For the 2002 tax year, the Department of Revenue of the State of Georgia (the "Department") determined that the unit value of CSXT's rail transportation property was $8.2 billion and that the fair market value of CSXT's taxable railroad operating property in Georgia was $514,862,671 (the "Proposed Valuation"). The Department presented that value to the State Board of Equalization for the State of Georgia (the "Board") for approval. The Board approved the Proposed Valuation and issued a Notice of Proposed Assessment dated November 25, 2002.

CSXT makes three claims under the 4-R Act based on the Department's Proposed Valuation. First, CSXT claims that the Proposed Valuation is excessive and discriminatory in that the Department assessed CSXT's rail transportation property for ad valorem tax purposes at a higher ratio of assessed value to true market value than the ratio applicable to other commercial and industrial property in Georgia in violation of 49 U.S.C. § 11501(b)(1). Specifically, CSXT claims that the true market value of its rail transportation property on a unitary basis for the 2002 tax year does not exceed $6 billion, and that the true market value of its taxable rail transportation in Georgia does not exceed $369,253,752. This valuation claim is based primarily on an appraisal done by Mr. Thomas Tegarden, whose credentials are impeccable.

Second, CSXT claims that it has been singled out for discriminatory tax treatment by the defendants for the tax year 2002 in violation of 49 U.S.C. § 11501(b)(4). In particular, CSXT claims the Department's assessment of other centrally-assessed property is not based on the fair market

value of those properties. CSXT also claims that it is the only major centrally-assessed taxpayer in Georgia that suffered a significant tax increase for the tax year 2002.

Third, CSXT contends that the defendants discriminated against it in violation of 49 U.S.C. § 11501(b)(4) because the Department's Proposed Valuation for the tax year 2002 improperly included its intangible property, while the intangible property of all other commercial and industrial taxpayers is excluded from taxation. CSXT argues that the Department's valuation methods improperly compound intangible value, and CSXT urges the court to order the Department to use a yield capitalization approach, which CSXT claims will minimize the inclusion of intangible assets in the Department's valuation.

The matter was tried by the court sitting without a jury from May 16, 2005, through May 25, 2005. The court took the case under advisement pending the filing of post-trial briefs. The following order constitutes the court's findings of fact and conclusions of law as required by Federal Rule of Civil Procedure 52.

Factual Background

I. *The Parties*

A. *CSXT*

CSXT, the taxpayer in this case, is a Class 1 interstate common carrier by rail that operates in more than 71 counties in Georgia. It is subject to the jurisdiction of the Surface Transportation Board ("STB").

CSXT is a wholly-owned subsidiary of CSX Corporation. CSX Corporation's stock is publicly traded. As of January 1, 2002, CSX Corporation also owned several other subsidiaries including: (1) CSX World Terminals; (2) CSX Intermodal,

Inc.;[1] (3) CSX Lines; (4) CSX Technology, Inc.; and (5) CSX Hotels, Inc.

As of the fiscal year ending December 28, 2001, CSXT accounted for 75% of CSX Corporation's total operating revenues and 78% of its operating income.[2] CSXT's operating revenues for that year alone amounted to $6.082 billion with an adjusted operating income of $803 million.

By the mid-1990's only three Class 1 railroads existed and competed for freight traffic in the eastern half of the United States: (1) Consolidated Rail Corporation ("Conrail"), (2) Norfolk Southern Corporation ("Norfolk Southern"), and (3) CSXT. In August 1998, the STB approved the joint acquisition of Conrail by Norfolk Southern and CSX Corporation. The acquisition included an outright buyout of Conrail's assets by Norfolk Southern and CSX Corporation for approximately $10.5 billion and the assumption of net debt of $1.9 billion.

In June 1999, CSXT began operating portions of Conrail's system. By January 1, 2002, CSXT was operating approximately 42% of the former Conrail system. At that time, CSXT provided rail freight transportation over a network of approximately 40,000 miles of track and 23,000 route miles.[3] CSXT's network included a route through the southeastern United States, including Georgia, as well as a route from the New York/New Jersey area down the east coast to Florida.

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[1] CSX Intermodal ("CSXI") moves trailers or containers on flat cars to trucks. In addition, CSXI operates 33 terminals across the United States. When CSXI moves intermodal traffic over CSXT's system, CSXI pays CSXT a "transfer price" of approximately $350 to $400 million annually for CSXI's use of CSXT's resources and routes.

[2] Operating income is operating revenues minus total operating expenses.

[3] The acquisition of Conrail added 4,400 miles of track to CSXT's rail system in the Northeast United States and Canada.

CSXT's rail transportation property consists of a variety of items, including land, rail, track material, stations, and equipment. CSXT also operates rolling stock and equipment that it leases. During the time period in question, CSXT had between 34,000 and 36,000 employees and operated between 230,000 to 240,000 freight cars on its system.

Maintaining a rail transportation system requires heavy investment in capital expenditures.[4] Mr. Lewis, a Vice President of CSXT, testified that for the calendar years 2000 and 2001, CSXT's total capital expenditures were between $800 and $900 million.

The acquisition of Conrail had a noticeable effect on CSXT's revenues. For example, in 1997, CSXT's unlevered free cash flow was $467 million. In 1998, after the STB approved the Conrail merger, CSXT's unlevered free cash flow plummeted to negative $115 million. In 1999, CSXT' s [sic] unlevered free cash flow again plunged to negative $309 million. By 2000-2001, some efficiencies were beginning to be realized, and CSXT's unlevered free cash flow rose by 154.9% in two years.[5]

Similarly, the Conrail merger also had an effect on CSXT's operating ratio.[6] CSXT's operating ratio prior to the acquisition of Conrail was 75.4%. After acquiring Conrail, CSXT's operating ratio rose to a high of 89.9% and then began to decline again (to a more profitable ratio) in 2001.

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[4] The term "capital expenditure" refers to purchases of depreciable assets with long lives.

[5] In 2001 and 2002, CSXT Surface Transportation had a positive cash flow of around $150 million. Mr. Lewis testified that the positive cash flow was primarily due to real estate sales of $325 million.

[6] The term operating ratio refers to the ratio of operating expenses to revenue.

Although the acquisition of Conrail had a negative effect on CSXT's financial success in the short-run, the evidence at trial showed that it was likely that some efficiencies would be achieved in the future due to the merger. In fact, even CSXT's own expert, Mr. Tegarden, testified that some costs may be eliminated, which would increase future net operating income.

The evidence at trial also showed that railroads face considerable competition from other modes of transportation, such as trucks. Unlike trucks, however, railroads have to pay for and maintain their own infrastructure. Beginning in 1980, this competition steadily forced rates down. Taking trucks off the highways was the stated goal of the Conrail merger. To that end, the Conrail merger created a huge growth opportunity for CSXT. For instance, in 2001, CSXT was able to move 350,000 truckloads of merchandise off the roads and onto their rails.

B. *The Defendants*

The defendants are the Board and its individual members, including Bart L. Graham, the State Commissioner of Revenue.

The appraised and assessed values of most property in Georgia are determined by county boards of assessors. The parties refer to this property as "locally-assessed" property. Pursuant to O.C.G.A. § 48-5-6, most locally-assessed property subject to taxation in Georgia is to be appraised for assessment purposes at its fair market value. After any such nonexempt locally-assessed property in Georgia is appraised at its fair market value, an assessment ratio of 40% is applied to the appraised value to derive the assessed value. It is this assessed value against which property tax is levied and collected.

Companies classified in Georgia as "public utilities" are commonly referred to as "centrally-assessed" taxpayers.

Centrally-assessed taxpayers include railroads, investor-owned electric utilities, investor-owned telephone companies, pipeline companies, and gas distribution companies. The State Revenue Commissioner issues proposed assessments of the operating and non-operating property of public utilities such as CSXT.

The Property Tax Division of the Department annually prepares a proposed assessment of CSXT's railroad transportation operating property for every Georgia county in which CSXT's taxable property is located.

II. *The Department's Proposed Valuation of CSXT*

In Georgia, the procedure for assessing rail transportation property is set forth in O.C.G.A. § 48-2-18. Under that statute, the Board approves an initial, proposed assessment of the taxpayer's property, and certifies that assessment to the counties in which the taxpayer owns taxable property. *Id.* § 48-2-18(c). *See also Telecom USA, Inc. v. Collins*, 260 Ga. 362, 364-65, 393 S.E.2d 235, 238 (1990) (discussing revised Georgia tax assessment procedures); *Colonial Pipeline Co. v. Collins*, 921 F.2d 1237 (11th Cir.1991) (same). Each county must then issue its final assessment to the taxpayer within 30 days; in doing so, "a county may, but is not required to, use the[ ] figures [provided by the Board] as the county's own tax assessment." *Colonial Pipeline*, 921 F.2d at 1240-41.

The Department used the unit rule method to value CSXT's railroad transportation operating property for 2002 ad valorem tax purposes. The unit rule method values the entire operating system of CSXT as a going concern and integrated whole irregardless of where it is located and without functional or geographic division of the whole into its component parts. A unit value determined pursuant to the unit rule method is meant to capture all of the operating assets

of the company whether owned or used. The parties agree that the unit rule method is appropriate under Georgia law.

Gregg Dickerson is the Program Manager in the Public Utilities Section of the Local Government Services Division of the Department. Mr. Dickerson first joined the Department in 1983 and spent ten years doing valuations pursuant to the unit rule method for centrally-assessed public utilities, including railroads. In 1993, he left the Department and went to work for Norfolk Southern railroad as a property tax manager, where his duties included reviewing and negotiating unit values with various states.

In the fall of 2001, Mr. Dickerson was approached by the then-director of the Department, Mr. Larry Griggers, who asked him to return to the Department. Mr. Griggers stated that he was concerned that the public utility digest for Georgia had decreased from 10% to 5% of the total state property tax digest since Mr. Dickerson's departure. Mr. Dickerson agreed to return, but stated that he would not come back for the purpose of "raising the numbers." He would only come back if Mr. Griggers' purpose was to "get[ ] the numbers right." Mr. Griggers agreed and Mr. Dickerson returned to work for the Department in September 2001. Mr. Dickerson was the individual responsible for preparing the valuation worksheets that served as the basis for the Department's Proposed Valuation of CSXT for the tax year 2002.

Applying the unit rule method, Mr. Dickerson first prepared a Railroad Valuation Worksheet. The Railroad Valuation Worksheet calculated CSXT's unit value using three valuation methods: (1) a stock and debt approach, (2) a discounted cash flow ("DCF") approach, and (3) a market

multiple approach. These different approaches yielded the following values:

Stock and Debt	$12.022 billion
DCF	$8.126 billion
Market Multiples[7]	$12.346 billion
	$10.769 billion
	$8.474 billion

After coming up with this range of values for CSXT, Mr. Dickerson selected $8.2 billion as the lower limit of what the going concern unit value of CSXT could reasonably be. He then used $8.2 billion as the foundation for the Department's Proposed Valuation.

After determining the unit value for CSXT, Mr. Dickerson then estimated a working capital adjustment of $400 million and deducted that from his unit value estimate of $8.2 billion to eliminate the effect of certain intangible assets. Next, Mr. Dickerson allocated the adjusted unit value estimate of $7.8 billion to the state of Georgia by using the percentage of Georgia road miles to system road miles. For the tax year 2002, the percentage so applied equaled 7.194059%, resulting in an allocated value of $561,136,602 for the state of Georgia.

To arrive at CSXT's proposed taxable fair market value in Georgia, Mr. Dickerson then deducted amounts for motor vehicles, exempt pollution control equipment, and exempt railroad lines. As a result, Mr. Dickerson determined that CSXT's taxable fair market value in Georgia for the tax year 2002 was $514,862,671 and presented this number to the Board.

Following the Board's approval, the Department issued a Notice of Proposed Assessment dated November 25, 2002 (the "Proposed Assessment"), to CSXT and to the counties in

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[7] The market multiple approach yielded three different values because the Department calculated three different "multiples."

which CSXT had taxable property. The Proposed Assessment included three components: (1) the portion of the Department's proposed taxable fair market value of CSXT's operating property in Georgia attributable to each county, (2) the level of assessment that the Board determined each county should use, and (3) a proposed assessment for each Georgia county in which CSXT had taxable property, which was derived by multiplying the county's distributed value by 40% or the prevailing level of assessment in that county.

After this litigation commenced, in November 2003, Mr. Dickerson prepared a complete appraisal of CSXT using essentially the same three valuation methods that he employed with the Proposed Valuation. The purpose of this appraisal was to provide the court with Mr. Dickerson's point estimate of CSXT's unit value, rather than a figure at the lower end of his range of fair market values.

Following the close of fact discovery in this case, Mr. Dickerson prepared a revised full appraisal of CSXT in support of the Proposed Valuation. The only difference between Mr. Dickerson's November 2003 appraisal and the revised appraisal involved a change in the calculation of the cost of equity used in deriving the weighted cost of capital. The range of values Mr. Dickerson arrived at in his second appraisal were:

As should be abundantly clear by this point, in reaching this conclusion, the Court was not persuaded by TKT's alternative arguments that Amgen failed adequately to describe the production of erythropoietin either by use of a human cell line or by activating the otherwise dormant endogenous erythropoietin gene. *See supra* note 51.

Stock and Debt	$12.128 billion
DCF	$10.960 billion
Market Multiples	$12.434 billion
	$10.871 billion
	$8.986 billion

Based on this range of values, Mr. Dickerson opined that the fair market system value of CSXT as of January 1, 2002, prior to adjustments for leases was $11 billion. Mr. Dickerson then added $807 million to this value to account for the value of CSXT's operating leases. He ultimately opined that the fair market unit value of CSXT was $11.807 billion.

III. *An Overview of the Parties' Valuation Approaches*

As noted above, in Georgia, as in most states, a railroad's operating property is valued for property tax purposes as a unit. Under the unit concept of value, the fair market value of the railroad is measured by appraising the whole property as a going concern. To determine the unit value of a company, the appraiser must first choose from and apply a variety of valuation methods.

There are three general approaches to valuing a company or property: (1) the sales comparison approach, (2) the income approach, and (3) the cost approach. The standard sales comparison approach determines the value of a property or company by examining and comparing actual sales of comparable properties or companies. Conversely, the cost approach determines the value of a property by totaling the original costs of the various components of the property, and then making adjustments to account for depreciation or obsolescence. The theory behind the income approach is that anyone who buys a company buys it only for the income the company will generate.

Mr. Dickerson's responsibilities in preparing proposed assessments for centrally-assessed property for the tax year 2002 included reviewing the valuation methods that had been used by the Department in the past. As a result of his analysis, Mr. Dickerson made certain changes to the valuation methods used for all centrally-assessed taxpayers subject to the unit rule method. Those changes, which were applied on

an across-the-board basis, included replacing the existing capitalized earnings approach with a DCF model. He also replaced what had been labeled as a direct capitalization approach with a market multiple approach.

For CSXT, Mr. Dickerson used three different valuation methods: (1) a stock and debt approach, (2) a DCF approach, and (3) a market multiple approach. In rough terms, the stock and debt method is a surrogate for the sales comparison approach. It assumes that the value of a company equals all of the outstanding debt owned by that company plus the company's equity. Similarly, the market multiple approach is also a substitute for the sales comparison approach. Under a market multiple approach, the appraiser derives market multiples from the stock prices of companies that are engaged in similar lines of business and compares those multiples with the subject company to determine the value of that company.

Unlike the stock and debt and market multiple approaches, the DCF approach is a version of the income approach. Under the DCF approach, the appraiser makes assumptions to project cash flows for the company for a designated number of years after the assessment date, and then discounts those expected cash flows to their present value. The appraiser then calculates a terminal or reversion value representing the value of the company at the end of the projection period. The total of the discounted cash flows during the projection period and the terminal value gives the appraiser his unit value for the company.

CSXT's valuation expert, Mr. Tegarden, also used three valuation methods to value CSXT: (1) a stock and debt approach, (2) a cost approach, and (3) a yield capitalization approach. The yield capitalization approach is another variation of the income approach. It can perhaps be described

as a cousin of the Department's DCF approach. For example, the Department's DCF model is expressed as:

$$V = \frac{(CF1)}{(1+k)} + \ldots \frac{(CFn)}{(1+k)} + \frac{T}{(1+k)}$$

Cfn = net cash flow for the year n, k = discount rate, T = terminal value, and n = year. Mr. Tegarden's yield capitalization approach is expressed by the formula:

$$V = \frac{I}{r}$$

I = income and r = discount rate.

Mr. Tegarden gave no weight to his stock and debt value, very little weight to his calculations under the cost approach, and primary weight to his yield capitalization value. Using this weighted scale, Mr. Tegarden picked approximately $6 billion as the unit value of CSXT.

Legal Analysis

I. *The 4-R Act*

The 4-R Act prohibits a state from "[a] ssess[ing] [sic] rail transportation property at a value that has a higher ratio to [its] true market value . . . than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to [its] true market value. . . ." 49 U.S.C. § 11501(b)(1). The 4-R Act also prohibits states from levying or collecting taxes based on such an assessment, or otherwise discriminating against rail carriers in taxation. *Id.* § 11501(b)(2)-(4). "Assessment" is defined in the 4-R Act as "valuation for a property tax levied by a taxing district." *Id.* § 11501(a)(1).

II. *Burden of Proof*

The burden of proof in a case brought under the 4-R Act is determined by state law. 49 U.S.C. § 11501(c). The 4-R Act

requires a district court to use the burden of proof generally applicable to civil proceedings. *See Burlington Northern Railroad Co. v. Bair*, 766 F.2d 1222, 1226 (8th Cir.1985); *Atchison, Topeka, and Santa Fe Railway v. Lennen*, 732 F.2d 1495, 1500 (10th Cir.1984). In Georgia, a preponderance of the evidence is "the essential quantum of evidence . . . necessary to satisfy the minds of the fact finders in civil cases." *Ocean Accident & Guarantee Corp. v. Bates*, 104 Ga.App. 621, 622, 122 S.E.2d 305, 307 (1961). Thus, CSXT' s [sic] burden is the preponderance of the evidence standard.[8]

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[8] The defendants contend that the court must accept their tax assessment as prima facie correct, and that the burden is on CSXT to show that their assessment is in error. The defendants' argument is based on their belief that the burden of proof applicable in this case is the same burden of proof used when a taxpayer litigates the assessment they received in Georgia. This is not, however, a case where CSXT is simply appealing the Department's assessment. This is a case brought under the 4-R Act and the court must determine the true market value of CSXT. CSXT, in turn, has the burden of proving by a preponderance of the evidence that the true market value of its property is $6 billion. To do this, CSXT presented two types of evidence. First, it criticized the Department's calculations. Second, it presented a valuation of its property by Mr. Tegarden. In a more typical case, the court would look at both Mr. Tegarden's appraisal and the Department's appraisal to determine the true market value of CSXT. If the court found by a preponderance of the evidence that CSXT's true market value was $6 billion, as proposed by CSXT, then the court would compare the Department's Proposed Valuation to CSXT's true market value to determine if discrimination occurred. However, as explained later in this order, the court cannot consider Mr. Tegarden's valuation because it was prepared using different valuation methods than the Department. The court, therefore, is limited to looking solely at CSXT's criticisms of the Department's valuation.

III. *Whether the Department Assessed CSXT's Operating Property in Georgia for the Tax Year 2002 in Excess of its True Market Value, Resulting in a Ratio of Assessed Value to True Market Value for CSXT's Property which Exceeds by More than 5% the Ratio of Assessed Value to True Market Value of Other Commercial and Industrial Property in Georgia*

A. *May CSXT Challenge the Department's Chosen Valuation Methods?*

In this case, the parties disagree over the proper way to calculate the value of CSXT under each valuation method. Significantly, the parties also disagree over which valuation method the Department should use to value CSXT.

One of the problems with subjecting complex issues like valuation to judicial determination is that the court generally must choose among the competing claims of experts. Unless the court performs its own appraisal, the court must rely either on CSXT's experts or the Department's experts. The court, of course, may adjust an expert's appraisal up or down based on other experts' critiques of the appraisal, but the starting point for judicial determination is always one appraisal or another, and each appraisal is based on a particular methodology that, to a large extent, predetermines the result. Thus, implicit in the court's holding is a decision as to the proper valuation method.

The evidence shows that all five approaches used by CSXT and the Department, the yield capitalization, DCF, stock and debt, market multiple, and cost approaches, are widely used to value property. The question, then, is whether the Department is free to choose among accepted valuation methods or whether the 4-R Act compels the use of one particular method.

The United States Supreme Court in *Burlington Northern Railroad Co. v. Oklahoma Tax Commission*, 481 U.S. 454,

463 n. 5, 107 S.Ct. 1855, 1861 n. 5, 95 L.Ed.2d 404 (1987), expressly left open the question of "whether a railroad may, in an action under [the 4-R Act], challenge the appropriateness of the accounting methods by which the state has determined the railroad's value, or is instead restricted to challenging the factual determinations to which the state's preferred accounting methods were applied." *Id.*

Since the *Burlington Northern* decision, several courts have answered this question. Perhaps the most followed decision is the Fourth Circuit's decision in *Chesapeake Western Railway v. Forst*, 938 F.2d 528, 533 (4th Cir.1991), *cert. denied*, 503 U.S. 966, 112 S.Ct. 1577, 118 L.Ed.2d 220 (1992). *See also Burlington Northern Railroad Co. v. Bair*, 815 F.Supp. 1223, 1228-29 (S.D.Iowa 1993) (following *Chesapeake* and holding that a railroad may not challenge the state's chosen methodology); *cf. Union Pacific Railroad Co. v. State Tax Commission of Utah*, 716 F.Supp. 543, 556-57 (D.Utah 1988) (holding that as long as the state's method has a rational basis and was not chosen for a discriminatory purpose, the court will not disturb the state's choice). In *Chesapeake*, the railroad brought an action challenging Virginia's "over the fence" method of valuing railroad property and arguing for use of the unit method. *Chesapeake*, 938 F.2d at 530. Relying primarily on the 4-R Act's legislative history, the Fourth Circuit concluded that the 4-R Act "does not provide a basis for railroads to challenge a state's preferred methodology for ascertaining the true market value of railroad property." *Id.* at 533; *see also Richmond, Fredericksburg & Potomac Co. v. Forst*, 4 F.3d 244, 250 (4th Cir.1993) ("[A] railroad may present independent evidence of the fair market value of its property, provided, of course, that it limits its evidence to factors that may properly be taken into account under the state's chosen methodology.").

As support for its argument that the court should allow it to challenge the Department's valuation methods, CSXT cites to

decisions from the Second and Ninth Circuit. Neither of these circuits, however, allowed a railroad to freely challenge the state's methodology. For instance, in *Consolidated Rail Corp. v. Town of Hyde Park*, 47 F.3d 473, 482 (2d Cir.1995), the Second Circuit held that the state must apply the "same valuation standard and methods to the railroad property as are used on the commercial and industrial properties to which [the railroad] is compared." The implicit holding in *Hyde Park*, therefore, is that a railroad cannot challenge the state's valuation methods as long as the state uses the same methods for other commercial taxpayers. Here, the evidence at trial showed that the Department used essentially the same valuation methods for CSXT that it used for other centrally-assessed taxpayers.

Similarly, while the Ninth Circuit allowed a railroad to challenge the state's chosen methodology, it also held that the state's chosen methodology is presumed correct and can be defeated only by clear, cogent, and convincing evidence. *Burlington Northern Railroad v. Department of Revenue of the State of Washington*, 23 F.3d 239, 241 (9th Cir.1994).

Although the Eleventh Circuit has yet to address this question, the court finds that the legislative history, which is admittedly rather thin, supports the Fourth Circuit's determination that the 4-R Act does not confer jurisdiction upon this court to order the Department to use a specific accounting method to determine the value of CSXT. The committee report on Senate Bill 927, one of several precursors to the 4-R Act, states that:

> [The bill] does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves. It merely provides a single standard against which all affected assessments must be measured in order to determine their relationship to each other. It is not a standard for determining value; it is a

> standard to which values that have already been determined must be compared.

S.Rep. No. 1483, 90th Cong., 2d Sess.App. B (1968).

Similarly, in hearings on House Bill 16245, another forerunner of the 4-R Act, Mr. Lanier, a railroad representative, testified that, "[t]he standards and methods of valuation that any state wishes to use would be totally unaffected by this legislation." *Chesapeake*, 938 F.2d at 531 (*citing* Hearing Before the Subcommittee on Interstate and Foreign Commerce on H.R. 16245, 91st Cong., 1st Sess. 138 (1970)). Thus, the legislative history suggests that the statute was not meant to require a state to use a particular accounting method, at least as long as the state's chosen methods are rational and were not chosen for a discriminatory purpose.

After eight days of trial, it is apparent to the court that valuation is an art, not a science. Valuing a business requires an appraiser to make "judgment calls," even under CSXT's yield capitalization method. Absent a willing buyer and a willing seller, the determination of true market value for purposes of ad valorem taxation is always an estimate, always an expression of judgment, and always a result built on "judgment calls." The appraisals in this case are good examples of this. Mr. Tegarden and Mr. Dickerson each used at least three different valuation methods to arrive at the market value of CSXT. Both Mr. Tegarden and Mr. Dickerson arrived at different conclusions as to the value of CSXT under each method that they utilized. For example, CSXT's own expert, Mr. Tegarden, arrived at the following three values for CSXT for the tax year 2002:

Cost Approach	$6.150 billion
Income Approach	$5.983 billion
Stock and Debt Approach	$9.637 billion

The $3 billion difference in Mr. Tegarden' s values makes clear that the determination of the true market value of CSXT in this case is, at best, an educated guess. The fact that the determination of CSXT's true market value is an educated guess weighs against the court requiring the Department to use a particular valuation method.

In addition to the fact that all appraisals are at best educated guesses, the court is unwilling to dictate a particular valuation method to the Department for other reasons. From the testimony of the Department's witnesses, the court concludes that the Department sincerely seeks to arrive at what it considers to be CSXT's true market value, and that, to that end, it constantly reevaluates its methods and changes them when the Department becomes convinced that they are erroneous. If this court were to conclude that the 4-R Act required the Department to adopt the yield capitalization method of valuation, it would prevent the Department from critically examining its appraisal methods and would discourage it from adopting new and better methods as they become accepted by the appraisal profession.

For all of these reasons, the court concludes that the 4-R Act does not generally allow a railroad to challenge the state's chosen methodology. As long as the Department's chosen valuation methods are rational and were not chosen for the purpose of discriminating against CSXT, the court will not second guess the Department's choice of methods.

Even if the court were forced to choose between competing valuation methods, the court finds that the Department's chosen methods have much to commend them. Not only does the Department consistently use essentially the same approach for all centrally-assessed property, but its valuation methods are based on historical and market data readily available to investors and to the defendants. All three of the Department's valuation methods are widely accepted and used by valuation experts. The fact that these methods are

widely used and accepted is evidenced not only by the testimony of the majority of experts, but also by the fact that they have been approved by other courts. *See, e.g., Bair*, 815 F.Supp. at 1228-29 (approving of the use of the stock and debt approach to valuing the BN railroad); *Burlington Northern Railroad Co. v. Department of Revenue of the State of Washington*, No. C90-5417, 1992 WL 201947, at *4-5 (W.D.Wash. Aug.13, 1992), *aff'd* 23 F.3d 239 (9th Cir.1994) (giving deference to the state's use of the stock and debt, DCF, and cost approaches).

(1) *Whether the Department's Chosen Valuation Methods Are Irrational*

The court finds that the Department's chosen valuation methods are rational. As noted above, the stock and debt approach, market multiple approach, and DCF approach have much to commend them. They are widely accepted and generally based on historic and market data readily available to the public and investors.

CSXT' s primary criticism of the Department's valuation methods is that they compound intangible values at a higher rate than CSXT's yield capitalization method does. For example, CSXT introduced testimony showing that stock prices include value attributable to intangible property. Because all three of the Department's valuation methods utilize stock prices derived from CSX Corporation, CSXT's parent company, CSXT argues that the Department's approaches are flawed.

The court agrees that stock prices include intangible value, whether it is "intangible influences" or "intangible property." By extension, therefore, any approach that utilizes stock prices includes some intangible value. Nevertheless, the fact that the Department's approaches include intangible value does not make their use irrational. Both parties' experts agree that the fair market value of a business is meant to

value what a willing buyer would pay for that business. Stock prices, thus, are particularly relevant for appraisal purposes because absent a recent sale of the business, the company's stock price is the only real example of what a willing buyer would pay for a share of that business.

The court also points out that CSXT's own valuation methods are not exempt from the same criticism. It is undisputed that CSXT's yield capitalization method relies to some extent on stock prices and includes at least some value attributable to intangible property.

(2) *Whether the Department's Chosen Valuation Methods Were Adopted for a Discriminatory Purpose*

The court also finds that the evidence at trial does not support the conclusion that the Department selected the DCF approach, the stock and debt approach, or the market multiple approach for the purpose of discriminating against CSXT. The evidence at trial showed that the Department utilizes essentially these same methods when valuing non-railroad centrally-assessed property.

Accordingly, the court concludes that CSXT cannot challenge the Department's chosen valuation methods in this case. This ruling, of course, does not prevent CSXT from challenging the manner in which the Department calculated the value of CSXT using its stock and debt, DCF, and market multiple approaches.

B. *Can the Court Consider Mr. Tegarden's Appraisal of CSXT?*

The court is required to weigh the evidence and make its own factual findings regarding the true market value of CSXT. The question then arises as to whether the court can consider evidence of the true market value of CSXT' s [sic] operating property determined by a valuation method not employed by the Department. The court finds that it cannot

do so in this case because the valuation methods chosen by the Department are rational and were not adopted for a discriminatory purpose.

The court must make its factual findings as to the value of CSXT using the methods utilized by the Department. Otherwise, the court will be, in effect, ordering the Department to use a different valuation method.

It is undisputed that the Department used a DCF approach, a stock and debt approach, and a market multiple approach to value CSXT. CSXT's expert, Mr. Tegarden, appraised CSXT using a yield capitalization approach, a stock and debt approach, and a cost approach. Mr. Tegarden testified that he placed no weight on his calculations under the stock and debt approach and little emphasis on his calculations under the cost approach. Therefore, the court concludes that Mr. Tegarden's appraisal is based primarily on the yield capitalization approach with some small emphasis on the cost approach.[9]

The court concludes that both the cost approach and the yield capitalization approach are different valuation methods than the Department's valuation methods. Although the yield capitalization approach is undoubtedly a cousin of the Department's DCF approach, the fact that it is truly a different valuation method is most aptly illustrated by the fact that CSXT spent much of its time at trial arguing that the court should order the Department to adopt the yield capitalization approach because the other methods used by the Department to value CSXT were flawed.

Because the yield capitalization and cost approaches are different valuation methods than the methods used by the

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[9] CSXT admits that the cost approach is not particularly reliable for use in valuing railroad assets because of the substantial obsolescence affecting railroad property. Pl.'s Post-Trial Br. at 22 [Doc. No. 113].

Department, the court cannot consider Mr. Tegarden's valuation of CSXT under these approaches. Since CSXT has introduced into evidence no other appraisal of its property using the valuation methods employed by the Department, the court must necessarily limit its analysis to the criticisms presented by CSXT as to the manner in which the Department calculated the value of CSXT under its DCF, stock and debt, and market multiple approaches.

C. *The Department's Appraisals*

Before the court reaches CSXT's criticisms of the Department's calculations, the court must first address the two appraisals created by the Department after the commencement of this litigation. As noted earlier, after this litigation commenced, the Department prepared two appraisals of CSXT. The purpose of these appraisals was to provide the court with Mr. Dickerson's point estimate of CSXT's unit value, rather than a figure at the lower end of his range of fair market values. The only difference between the two appraisals was a change in the calculation of the cost of equity used in deriving the weighted cost of capital.

The fact that the Department created two appraisals significantly complicates this case. The Department urges the court to disregard its original Proposed Valuation and hold that the actual fair market unit value of CSXT is $11.807 billion, which is the value derived from Mr. Dickerson' s [sic] revised appraisal. CSXT, however, focused the majority of its time at trial and in its post-trial briefs challenging the Department's Proposed Valuation.

The court has considered the Department's revised appraisal. As noted earlier, in its revised appraisal, the Department changed the way it calculated the cost of equity used in deriving the weighted cost of capital for CSXT. It appears to the court that the Department created this new method of calculating the cost of equity in late 2003 or early 2004 and,

thus, did not apply this formula to any other taxpayer in 2002. The court questions the relevancy of the revised appraisal for use in this lawsuit. The methods used were not applied to other taxpayers for the year 2002, and the revised appraisal was not used by the Department in assessing the values at issue here. The controversy before the court is the methods and the amounts used, not what could have been used. The court's analysis and approval (or disapproval) of the revised appraisal essentially amounts to an "advisory" opinion. Further, applying this new method of calculating the cost of equity to CSXT when it was not used for any other taxpayer would be inherently discriminatory. Accordingly, the court will focus the remainder of this order on the Department's Proposed Valuation.

D. *CSXT's Criticisms of the Department's Calculations*

As noted above, the Department utilized three methods for determining the fair market value of CSXT: (1) the stock and debt approach, (2) the DCF approach, and (3) the market multiple approach. Each of these approaches yielded a different unit value for CSXT. From this range of values, Mr. Dickerson then chose a number, $8.2 billion, that was closest to the lowest value in that range. The $8.2 billion unit value became the foundation for the Department's Proposed Valuation.

CSXT challenges the calculations made by Mr. Dickerson under his Proposed Valuation on four grounds. First, CSXT claims that the Department made errors in its DCF analysis. Second, CSXT claims that the Department calculated excessive stock and debt figures. Third, CSXT claims that the Department utilized excessive market multiple figures. Finally, CSXT claims that the Department improperly double-counted the value of CSXT's leased equipment.

(1) *CSXT's Criticisms of the Department's DCF Analysis*

To arrive at the DCF value of CSXT, the Department first calculated CSXT's anticipated future operating free cash flows for a ten-year period from 2002 to 2011 based on projections regarding the growth rate of CSXT's revenues, expenses, and capital expenditures. The Department then calculated a terminal value for CSXT (i.e., what a purchaser would expect to pay for the company at the end of the period). Next, the Department discounted this cash flow to January 1, 2002, using as the discount rate a 9.90% after-tax average weighted cost of capital. This calculation yielded a figure of $7,518,317,142, to which the Department added an amount for leased equipment of $607,976,209 to come up with a DCF value of CSXT of $8,126,293,350.

In particular, the Department's DCF model projected an increase in CSXT's cash flow of 69% from 2001 to 2002. The Department's model also projected a declining growth rate in cash flows from 5.32% in 2003 to 3.58% in 2011 and then assumed a constant terminal growth rate of 6.3% from 2011 into perpetuity. In addition, the Department assumed a 2% growth in revenues per year and projected that CSXT could achieve an 80% operating ratio by 2011.

According to CSXT, several of the assumptions in the Department's DCF model are erroneous because they allegedly have no basis in the historic record of CSXT's performance. In particular, CSXT claims that the Department erroneously projects: (1) a 69% increase in cash flow from 2001 to 2002, (2) a 6.3% terminal growth rate, and (3) an operating ratio of 80% by 2011. CSXT argues that these allegedly erroneous financial projections cause the Department's DCF model to overstate the value of CSXT.

(a) *The Department's Selection of 69% as the First Year's Cash Flow*

As noted above, the first year of the Department's DCF model assumes that CSXT's cash flow will increase by 69% over CSXT's actual cash flow for 2001. CSXT argues that this increase is bizarre and unsupported by the record. CSXT, however, introduced no evidence at trial as to what increase, if any, the Department should have projected or how that change would have affected the Department's value. In fact, instead of presenting testimony as to what the percentage increase or decrease the Department should have used and how changing that number affects the Department's DCF value for CSXT, CSXT argued that the court should correct the Department's projected terminal growth rate.

Regardless, the court finds that a 69% increase in projected cash flow from 2001 to 2002 is not bizarre. The evidence at trial showed that CSXT' s [sic] cash flow from 1991-2001 increased annually from 5.6% to 154.9% and sometimes declined. In fact, from 2000 to 2001, CSXT's unlevered free cash flow increased by more than 100%. Furthermore, as noted by CSXT' s [sic] expert at trial,[10] it is likely that some efficiencies may be achieved in the future due to the integration of CSXT and Conrail. These efficiencies will likely increase cash flow and reduce costs.

(b) *The Department's Selection of 6.3% as the Terminal Growth Rate*

CSXT next argues that the Department's decision to choose 6.3% as the terminal growth rate is excessively optimistic. CSXT points out that 6.3% is much higher than the growth rate that the Department projected for the years 2003-2011.

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[10] This statement was made by Mr. Tegarden in the context of explaining how he came up with $700 million as his estimate of CSXT's future net operating income.

CSXT also argues that the logical incongruence of the Department's terminal growth rate is indicated by the fact that the Department estimated that CSXT' s [sic] revenue would grow at only 2%. CSXT points out that if revenue grows at only 2%, while free cash flow (roughly revenue minus expenses) grows at 6.3% then at some point in time expenses would have to decline and become negative to sustain the 6.3% growth in free cash flow.

The court finds that the Department's decision to adopt a 6.3% terminal growth rate is not erroneous. First, to the extent that CSXT's experts opined that 6.3% was an unrealistic terminal growth rate, the court finds that their testimony was not credible. Second, the court notes that none of CSXT's experts testified as to what a proper terminal growth rate should be. At most, these experts suggested that the Department should have adopted 3.5% or 4.5% as the terminal growth rate. These "suggested" rates also suffer from some of the same infirmities that the rate selected by the Department does. For example, if revenues grow at 2%,[11] but free cash flow grows at any number higher than 2% (e.g., 3.5% or 4.5%) then eventually costs will have to decrease to a negative number.

(c) *The Department's Projected Operating Ratio*

CSXT also criticizes the operating ratio forecasted in the Department's Proposed Valuation. CSXT points out that it did not achieve its planned operating income or ratio from June 1999-December 2002. CSXT also presented evidence from Mr. Lewis, CSXT's Vice President of Finance, that the

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[11] Because the growth rate for revenue slowed to .4% per year from 1996 to 2001, CSXT also argues that the Department's projected growth rate of 2% per year for revenue is unduly optimistic. The court disagrees. CSXT admits that a 2% annual growth in revenue is not inconsistent with national trends for railroads between 1991 and 2001.

business risks facing the railroad industry make it "difficult to imagine . . . hav[ing] a lower operating ratio."

While it is true that CSXT did not achieve its planned operating ratios from 1999-2002, this fact alone does not indicate that the target operating ratios predicted by the Department were erroneous. Among other things, the Department estimated that CSXT would achieve an operating ratio of 80% by the year 2011. Eighty percent is consistent with CSXT' s strategic plan, its presentations to bond rating agencies, and the average historic operating ratios achieved by railroads, including CSXT, from 1995-2001. In fact, in 1998, prior to CSXT's acquisition of Conrail, CSXT achieved a 78.6% operating ratio. By 2001, CSXT's operating ratios had begun to decrease from a high of 89.9% in 2000. CSXT's 2001 Annual Report noted this change in trend stating, "With revenues expected to go up this year, the railroad's operating ratio, i.e., total costs as a percentage of total revenues, should improve considerably." Thus, it was reasonable for the Department to project that CSXT would achieve an operating ratio of 80% by the year 2011.

(2) *CSXT's Criticisms of the Department's Stock and Debt Analysis*

The Department determined the stock and debt value of CSXT by taking normalized year-end price data from Standard & Poor's Stock Guide and information from CSX Corporation's 2001 Annual Report. The Department concluded that the total market value of CSX Corporation's stock, its long-term debt, and the excess of current liabilities over current assets as of January 1, 2002, was $15,219,745,138. The Department next performed several calculations to determine what portion of this total was properly attributable to CSXT. The ratios the Department calculated were: 74. 91%, 81. 89%, 77. 93%, and 75. 47%. The Department selected 75% as a conservative number within that range. The Department then multiplied

$15,219,745,138 by 75% to come up with the portion of CSX Corporation's debt and equity which was allocable to CSXT. After adding $607 million for leased equipment, the Department arrived at $12,022,785,209 as the stock and debt value of CSXT.

In CSXT' s post-trial brief, CSXT points out a host of problems with the stock and debt approach generally, as opposed to problems with the Department's calculation of CSXT's stock and debt value. For example, CSXT argues that there is a disconnect between stock and debt values and the value of the taxable assets being valued in this case. CSXT points out that a company's stock price inevitably includes intangible values and assets not in existence on the date of the assessment, whereas an appraiser is only supposed to value tangible operating assets that are in existence as of the date of the appraisal.

As the court has previously indicated, it was proper for the Department to use the stock and debt approach to come up with a range of values for CSXT. *See Bair*, 815 F.Supp. at 1239 (approving of the use of the stock and debt approach in the appraisal of a railroad). The court, moreover, has already held that CSXT may not challenge the Department's chosen valuation methods.

In addition to criticisms of the stock and debt approach generally, CSXT argues that the stock and debt approach is not appropriate in this case because CSXT is not a publicly traded company. Although the stock of CSX Corporation is publicly traded and CSXT is wholly-owned by CSX Corporation, CSXT claims that it is difficult to identify a stock value attributable to CSXT' s [sic] railroad assets.

The court finds this argument unpersuasive. The mere fact that the Department must calculate and allocate a portion of CSX Corporation's stock to CSXT does not justify rejecting the Department's stock and debt value. Notably, CSXT does

not argue that the Department allocated the wrong proportion of CSX Corporation's equity to CSXT. In fact, it appears to the court that the parties agree that CSXT constitutes between 75-80% of CSX Corporation's total equity. CSXT's own expert, Mr. Tegarden, attributed 78.9% of CSX Corporation's total equity to CSXT when he calculated the discount rate in his yield capitalization approach.[12]

CSXT's final argument is that the Department erred by failing to make an adjustment to reflect the liquidity of stocks, as opposed to assets. CSXT points out that it is easier to buy a few units of stock, as opposed to the entire operating assets of a railroad. Because it is easier to buy stock, shares of stock reflect a liquidity premium that is not shared by the hard assets of a company.

Even if the court were to conclude that CSXT was correct, CSXT failed to present any expert testimony attesting as to how large an illiquidity discount the Department should have applied. At most, Mr. Tegarden' s [sic] report suggests that an illiquidity discount plus an adjustment for minority interests of 37.5% may be appropriate.[13] Pl.'s Ex. 1 at 60, n.

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[12] In other parts of its brief, CSXT suggests that the Department may have miscalculated the amount of debt attributable to CSXT. Even if the court were to accept this criticism, as well as CSXT's liquidity criticism described later in this opinion, according to the court's calculations the unit value of CSXT would be approximately $7.6 billion. This number is much higher than the $6 billion value proposed by CSXT.

Further, the court notes that the value of CSX Corporation's debt is $8.296 billion. If the court were to attribute 75% of CSX Corporation's debt to CSXT, the value of CSXT would be $6.2 billion. If, as CSXT claims, the value of CSXT was $6 billion, CSXT would have a negative equity value. CSX Corporation, however, held investment grade bond ratings implying a profitability level in excess of that needed to pay both current interest expenses and the principal balance of debt.

[13] If the court were to assume that CSXT's stock has a value in the market that is 37.5% higher than its underlying assets, according to the court's calculations the Department's stock and debt value of CSXT

46 ("Some studies have suggested that the effect of these two adjustments would be a reduction of the stock prices by approximately 37.5%."). This statement, however, is not specific to CSXT, nor does the court construe it as Mr. Tegarden's opinion regarding the actual illiquidity discount that should be applied to CSX Corporation's stock. In fact, Mr. Tegarden failed to include an illiquidity discount when arriving at his own stock and debt value.[14]

Nor is the court convinced that an illiquidity discount should be applied here. While stocks are undoubtedly more liquid than the entire operating assets of CSXT, buying the entire operating assets of a company gives the purchaser something that buying a few shares of stock cannot give him: control. One of CSXT's experts, Dr. Heaton, testified that an acquiring company will sometimes pay a control premium when the acquiring company believes that they can add value (create synergy) to the existing company. To the extent that any illiquidity discount may have been necessary, it may also have been completely offset by the necessity of adding a control premium.

(3) *CSXT's Criticisms of the Department's Market Multiple Analysis*

For the Department's market multiple approach, the Department identified six comparable railroads: (1) Burlington Northern, (2) Canadian National, (3) Canadian Pacific, (4) CSX Corporation, (5) Norfolk Southern, and (6) Union Pacific. The Department then multiplied the number of shares for these railroads by their year-end stock price to come up with the value of their equity. Next, the Department

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would be approximately $9.3 billion, much higher than Mr. Tegarden's $6 billion value for CSXT.

[14] In his appraisal report, Mr. Tegarden valued CSXT under the stock and debt approach at $9.637 billion. He testified that he gave little to no weight to this value because it did not include an illiquidity discount.

totaled the book value of the debt of these railroads, added the value of their equity, and subtracted cash items to derive each railroad's total market capitalization number. The Department then divided the total market capitalization number for each railroad by three different measures of income: revenues, EBIT,[15] and EBITDA.[16] This resulted in "multiples," which the Department applied against the same measures of income for CSXT to estimate the value of CSXT. The Department's market multiple values of CSXT were: (1) $12,246,460,000; (2) $10,769,011,960; and (3) $8,474,781,660 respectively.

CSXT primarily complains that the Department's calculation of its market multiple values is erroneous because the Department failed to make adjustments to its calculations to account for differences between these companies and CSXT. For example, CSXT argues that the Department failed to account for differences between the size of the comparator railroads and CSXT, whether they are eastern or western railroads, and the total amount of their assets. According to CSXT, if the Department had made the appropriate adjustments to reflect the differences between those railroads and CSXT, the appropriate market multiple value of CSXT would be approximately $6.08 billion.

Although the court applauds the Department's use of publicly traded Class 1[17] major railroads as comparable companies, the court finds that the Department erred when it failed to make adjustments to the size of the comparator companies. CSXT, however, has failed to introduce

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[15] "EBIT" stands for "earnings before interest and tax."

[16] "EBITDA" stands for "earnings before interest, tax, and depreciation."

[17] As noted by Mr. Tegarden, the two Canadian railroads, Canadian National and Canadian Pacific, have enough revenue to be considered Class I railroads if they were U.S. companies.

sufficient evidence for the court to determine what the appropriate adjustments should have been. At trial, CSXT introduced into evidence Plaintiff's Exhibit 51, which purports to adjust the values of Burlington Northern, Norfolk Southern, and Union Pacific to account for their size in comparison to CSXT. In addition to the fact that it does not make adjustments for all of the railroads used by the Department, it is not clear to the court whether the exhibit properly adjusts CSXT' s [sic] size to account for the purchase of Conrail. Nevertheless, because the Department erred in calculating its market multiple approach, the court will disregard the values the Department arrived at under its market multiple approach.

(4) *CSXT's Criticisms of the Department's Add-Back to Account for CSXT's Leased Equipment*

CSXT, like most railroads, leases substantial numbers of "rolling stock," such as locomotives and freight cars. The Conrail transaction was also structured using leases. CSXT uses operating leases to pay for various Conrail road assets. To account for this leased equipment and the Conrail road assets, the Department added $607 million to the unit value of CSXT under each of its valuation methods.

According to CSXT, the addition of $607 million to account for CSXT's leased assets is unnecessary because the Department's unit value of CSXT under all three valuation methods includes the value of all operating property owned or used by CSXT, including its leased assets. CSXT also argues that if the Department was going to treat CSXT's leased assets as if they were owned, the Department should have recognized that CSXT's capital expenditures would have increased if CSXT purchased its leased assets. If capital expenditures increased, then CSXT's cash flow would have been lower. The failure to make this adjustment to capital expenditures results in double counting the value of the leased assets.

In response, the Department points out that CSXT's operating leases are off-balance sheet financing. Because the operating leases do not show up on CSXT's balance sheet, the full value of the operating leases are not captured in CSXT's stock and debt prices or in the Department's income approach, unless certain adjustments are made.

After much deliberation, the court concludes that the Department did not improperly double count CSXT's leased assets. In particular, the court finds Dr. Ifflander and Mr. Dickerson's testimony on this issue credible.

There are two types of leases: capital leases and operating leases. A capital lease generally lasts for the life of an asset and the lease can be renewed at the end of the asset's life or the asset may be acquired at a favorable price. An operating lease usually lasts for a period of time much shorter than the actual life of the asset, and the present value of lease payments is generally much lower than the actual price of the asset. At the end of the life of the operating lease, the equipment usually reverts back to the lessor.

Under standard accounting rules, a capital lease is treated like a purchase. It shows up on a company's books as an asset, and the lease obligations show up as a liability or debt. Operating leases, on the other hand, do not show up on a company's books as an asset or a debt—they are off-balance sheet.[18] Instead, payments for operating leases show up as cash outflows from operations.[19]

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[18] The term "off-balance sheet" debt has been the focus of much attention in the last few years due to the Enron scandal. One of the principal ways in which Enron was able to deceive investors as to its value was by engaging in extensive off-balance sheet financing transactions, which shifted debt off Enron's balance sheet, making the company's balance sheet look far stronger than it actually was. *See* Lawrence E. Mitchell, *The Sarbanes-Oxley Act and the Reinvention of Corporate Governance?* Vill. L.Rev. 1189, 1212 (2003).

[19] "Off-balance sheet financing has been used for many years as a source of capital financing for acquiring heavy equipment, especially

When a lease arrangement is treated as off-balance sheet financing, the court is satisfied that there are "real current or future cash flow consequences." *See* 1 D.R. Carmichael & Paul Rosenfield, ACCOUNTANTS' HANDBOOK 33 (10th ed.2003). There are also consequences for reported earnings, book value of debt and capital, and return ratios for the company. The court finds that operating[20] and net income are lower, debt and capital for the firm are understated, and return on equity and capital are much higher. Unless an adjustment is made to the income statements to treat CSXT's leased Conrail road assets as if they were owned, the estimated market value CSXT will be understated.[21] In this case, the Department properly made such an adjustment—$607 million

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aircraft. . . ." John C. Murray, *Recharacterization and Title Issues in Synthetic Leasing Transactions*, 479 Practicing L. Inst./Real Est. Handbook 889 (2000).

[20] Operating income is a key input in both parties' valuation methods, but especially the DCF method.

[21] The court is aware of the fact that the Southern District of Iowa in *Burlington Northern Railroad Co. v. Bair*, 815 F.Supp. 1223, 1231 (S.D. Iowa 1993), reached a seemingly different conclusion. Although the *Bair* decision is not binding upon this court, the court points out that the *Bair* court's analysis on this issue is rather perfunctory. Further, in *Bair*, the court appears to have held that because commercial and industrial personal property is exempt from taxation, adding it back to the state's unit value estimations improperly double-counts the value of the leased rolling stock. *Id.* at 1231. In Georgia, however, taxable property is defined as "all real property, including but not limited to leaseholds, interests less than fee, and all personal property. . . ." O.C.G.A. § 48-5-3. Furthermore, Georgia law also states that a railroad's rolling stock and other personal property appurtenant to the rolling stock shall be taxed on "as much as the whole value of the rolling stock and personal property as the length of the railroad in this state bears to the whole length of the railroad, without regard to the location of the head office of the railroad. . . ." O.C.G.A. § 48-5-520. Thus, there does not appear to be a comparable tax exemption in Georgia.

to the unit value of CSXT under each of the Department's valuation methods.[22]

E. *The Court's Conclusions Regarding the True Market Value of CSXT*

After parsing through days of expert testimony, the court concludes that the Department's DCF value as set out in its Proposed Valuation is the most accurate indicator of CSXT's unit value. As a result, the court holds that, for purposes of applying the 4-R Act to the defendants' assessments of CSXT, the true market unit value of CSXT for the tax year 2002 was $7,726,293,350.[23]

The court finds that the portion of CSXT's true market value that should be allocated to Georgia for the tax year 2002 is 7.194059%. The true market value of CSXT's taxable rail transportation property in Georgia for the tax year 2002, therefore, was $509,560,171.[24]

Determining the true market value of CSXT does not end the inquiry. CSXT is only entitled to relief if the "ratio of [its] assessed value to [its] true market value . . . exceeds by at least 5% the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." 49 U.S.C. § 11501(c). The parties have stipulated that the ratio of assessed value to true market

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[22] Except for arguing that no adjustment is necessary, CSXT has offered no evidence as to what the amount of the adjustment should have been.

[23] The court arrived at this number by taking the Department's $8,126,293,350 DCF value for CSXT and subtracting $400 million to account for CSXT's intangible property.

[24] The court reached this number by taking the $7,726,293,350 true market unit value of CSXT and allocating 7.194059% to Georgia. The court then deducted $4,156,193 to account for CSXT's motor vehicles, $2,907,467 to account for pollution control, and $39,210,271 to account for W & A exempt line.

value for all other commercial and industrial property in Georgia is 40%. For CSXT to succeed against the defendants, therefore, the ratio of assessed value to true market value of CSXT's rail transportation property in each assessment jurisdiction must be at least 42%.[25]

Regardless of whether the assessment jurisdiction is the county or the state, the ratio of assessed market value to true market value for CSXT's rail transportation property is less than 42%. As a result, the court concludes that the defendants have not discriminated against CSXT in violation of 49 U.S.C. § 11501(b)(1).

IV. *Whether the Defendants Singled Out CSXT for Discriminatory Treatment by Applying a Higher Valuation Approach to CSXT's Property than the Valuation Approach Applied to Other Centrally-Assessed Taxpayers in Georgia for the Tax Year 2002 in Violation of 49 U.S.C. § 11501(b)(4)*

The provisions of 49 U.S.C. § 11501(b)(4) forbid the imposition of any tax that discriminates against a railroad. The United States Supreme Court has held that when railroads are singled out for discriminatory treatment, discrimination under 49 U.S.C. § 11501(b)(4) has occurred. *See Department of Revenue of Oregon v. ACF Industries, Inc.*, 510 U.S. 332, 346-47, 114 S.Ct. 843, 851, 127 L.Ed.2d 165 (1994).

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[25] Section 11501(c) states that relief may be granted under this section "only if the ratio of assessed value to true market value of rail transportation property exceeds by at least 5% the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." Once the 5% threshold is satisfied, the court is empowered to prevent all discrimination against the railroad. The 5% threshold is calculated by measuring 5% of 40%, which yields two percentage points. *See Southern Railway Co. v. State Board of Equalization*, 712 F.Supp. 1557, 1565-66 (N.D.Ga.1988).

CSXT claims that it has been singled out for discriminatory treatment because the Department did not attempt to assess the fair market value of other centrally-assessed taxpayers. Instead, CSXT claims that other centrally-assessed taxpayers are being taxed at whatever the Department determines is the lowest estimate of value that it could reasonably accept. CSXT argues that it is entitled to taxation on the same basis as these other centrally-assessed utilities-taxation based on the lowest possible value.

CSXT also argues that it has been treated differently than Norfolk Southern, the only other major railroad in Georgia. As evidence of this discrimination, CSXT points out that the Department consistently valued Norfolk Southern higher than CSXT, yet in the course of other litigation, the Department agreed to value Norfolk Southern at less than $8.2 billion for the tax year 2002.

A. *Whether CSXT Has Been Taxed Differently Than Other Centrally-Assessed Taxpayers*

CSXT first claims it has been singled out for discriminatory treatment because the Department's assessments of non-railroad centrally-assessed taxpayers are not based on the appraiser's opinion of the fair market value of those properties. In support of this claim, CSXT points out that Mr. Dickerson testified that he prepared proposed assessments for non-railroad utilities that represented the "lowest number he could come up with" and a "number at the lower end of his range of fair market value." Presumably because CSXT can come up with a lower number for its value than the Department, CSXT argues that it was treated differently than other centrally-assessed taxpayers.

The court finds CSXT' s [sic] argument unpersuasive. The evidence at trial showed that in preparing the Department's proposed valuations of CSXT and other taxpayers subject to the unit rule method, Mr. Dickerson first determined the

range within which he thought a particular company's fair market value could lie and then chose a number at the lower end of this range. CSXT was treated in the same manner as other public utilities; Mr. Dickerson came up with a range of values for CSXT and then picked a number that was closest to the lower end of that range. Further, the evidence at trial showed that Mr. Dickerson used essentially the same valuation methods to determine the unit value of all taxpayers subject to the unit rule method. The court finds Mr. Dickerson' s [sic] testimony on this issue to be credible.

Moreover, the fact that CSXT could come up with a lower number than the Department is meaningless. The Department did not base its valuation of other centrally-assessed taxpayers on the lowest number those taxpayers could come up with.[26] Instead, centrally-assessed taxpayers were taxed at the lowest number that Mr. Dickerson could come up with, just as CSXT was.

As further evidence that CSXT has been singled out for discriminatory treatment, CSXT argues that the Department's Proposed Valuation for 2002 is 47.1% higher than CSXT's 2001 assessment, whereas other non-railroad centrally-assessed taxpayers suffered only minimal increases. According to CSXT, this large increase was primarily caused by the exceedingly high terminal growth rate that Mr. Dickerson used in his DCF approach.

The fact that CSXT' s [sic] 2002 assessment was 47.1% higher than its 2001 assessment, and that this percentage increase is much higher than the percentage increase of other centrally-assessed taxpayers, does not in and of itself show that CSXT has been discriminated against. An equally likely proposition is that CSXT was undervalued in 2001. Further,

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[26] The court has no doubt that other centrally-assessed taxpayers could have come up with values lower than Mr. Dickerson' s proposed valuation of their property.

absent evidence of the fair market value of CSXT in 2001 or the fair market value of other taxpayers in 2002, the court cannot determine that CSXT has been singled out for discriminatory treatment.

Mr. Dickerson, moreover, testified that the largest part of the increase in CSXT's 2002 assessment was due to a change he instituted that year for all railroads, which was not needed for non-railroad public utilities. Specifically, he began using income data taken from CSX Corporation's annual reports instead of CSXT's R-1[27] reports to project future cash flows in his DCF analysis. Because those income figures can differ significantly from each other, the choice of which to use can greatly affect the DCF indicator of value. The evidence at trial showed that CSX Corporation's annual reports reflect management's view of CSXT's financial performance.

Finally, CSXT argues that the Department's treatment of other centrally-assessed taxpayers for the tax year 2004 is potent evidence that CSXT was singled out in 2002. In the tax year 2004, Mr. Dickerson devised a new way of calculating the risk premium for centrally-assessed taxpayers, which he then applied to his valuation worksheets for the tax year 2004. This new calculation increased the Department's initial valuation of the majority of centrally-assessed taxpayers, which, in turn, caused a "stir." The Department, in an attempt to avoid litigation, had a meeting with six representatives from centrally-assessed taxpayers, including CSXT. At the conclusion of the meeting, CSXT and the other five companies agreed that for the tax year 2004, all centrally-assessed taxpayers would receive an assessment equal to their assessment for the previous year or the average of their past three years of assessments, whichever was greater. For 2004, CSXT was assessed at $6.5 billion, a

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[27] An R-1 report is a report made by a railroad, such as CSXT, to the STB.

slight increase over the Department's 2001 assessment. Because the Department reverted to CSXT's 2001 values in 2004, CSXT argues that this is an indication that CSXT was singled out for different tax treatment in 2002 and 2003.

The Department's 2004 assessment of CSXT indicates little about the Department's 2002 valuation of CSXT. The Department negotiated an agreement with all public utilities in 2004 to avoid litigation. The agreement mandated that these taxpayers receive an assessment equal to their assessment for the previous year or the average of their past three years of assessments. As a practical matter, the Department could not have used either formula for CSXT because CSXT had filed suits challenging the Department's 2002 and 2003 valuations. The only avenue left to the Department was to revert to CSXT's 2001 assessment.

B. *Whether CSXT Has Been Treated Differently Than Norfolk Southern*

CSXT next argues that it has been treated differently than the only other major railroad in Georgia, Norfolk Southern. Like CSXT, Norfolk Southern filed suit against the defendants challenging the Department's 2002 assessment. The Department, however, settled Norfolk Southern's lawsuit and agreed to only minimal increases in value over the Department's 2001 assessment of Norfolk Southern. Ultimately, this meant that Norfolk Southern's 2002 value in Georgia was less than $8.2 billion.

CSXT argues that valuing Norfolk Southern less than CSXT for the tax year 2002 is wrong and discriminatory. CSXT points out that the Department consistently valued Norfolk Southern higher than CSXT for the tax years 2002-2004 and consistently projected higher cash flows for Norfolk Southern. If the Department truly believed that Norfolk Southern was worth more than CSXT, how, asks CSXT, could the Department assert in this suit that CSXT' s [sic]

value is higher than the agreed-to value of Norfolk Southern for the tax year 2002?

The court finds CSXT' s arguments unpersuasive. Nothing in the 4-R Act requires the court to compare the treatment of CSXT to just one company, another railroad. In *Atchison, Topeka, and Santa Fe Railway,* 78 F.3d at 442, the railroad argued that the court could measure whether Arizona's tax statutes discriminated against it solely by looking at the treatment of other motor carriers, as opposed to comparing all commercial and industrial taxpayers. The Ninth Circuit rejected this argument stating, "Although subsection(b)(4) is silent as to the proper comparison class, congressional intent behind the 4-R Act dictates that the comparison class of 'other commercial and industrial taxpayers subject to the tax' be used." *Id.*

The court finds the logic of the Ninth Circuit persuasive. By narrowing the comparison class to just one company, CSXT attempts to greatly expand the reach of the 4-R Act and increase the likelihood of future litigation. Accordingly, the court finds that it is improper to compare CSXT's treatment to just one other company, Norfolk Southern, for purposes of determining whether CSXT has been discriminated against in violation of the 4-R Act.

Even if it was proper to compare solely CSXT and Norfolk Southern, the court still finds that CSXT has not been singled out for discriminatory treatment. CSXT did not present any evidence that it was treated differently than Norfolk Southern when the Department made its initial proposed valuation of Norfolk Southern. If anything, the fact that Norfolk Southern also filed suit challenging the Department's proposed valuation suggests that Norfolk Southern was treated similarly to CSXT.

In addition, the fact that the Department ultimately settled with Norfolk Southern does not compel the court to conclude

that CSXT was treated differently from Norfolk Southern. Lawsuits are settled for numerous reasons, including the need to allocate scarce legal resources differently.

V. *Whether the Department Improperly Included the Value of CSXT's Intangible Property in Its Proposed Valuation in Violation of 49 U.S.C. § 11501(b)(4)*

CSXT's last claim is that the Department's Proposed Valuation includes amounts attributable to intangible property that is not taxed to locally-assessed taxpayers, resulting in a violation of 49 U.S.C. § 11501(b)(4). When a railroad is valued as a unit on a going concern basis, it is undisputed that the unit value of that railroad necessarily includes all of the railroad's assets, both tangible and intangible. The trend in a majority of states, however, is to exclude intangible property from ad valorem taxation. In 1996, the state of Georgia followed this trend and repealed its ad valorem tax on intangible property. *See* O.C.G.A. § 48-6-21. Thus, the intangible property of CSXT is not taxable in Georgia.

As an initial matter, the court must address the definition of the term "intangible property." Intangible property is generally defined as property that lacks a physical existence, such as stock options and business goodwill. *Black's Law Dictionary* 1253 (8th ed.2004). The court is not aware of any decision by the Georgia Department of Revenue or by Georgia courts that articulates a list of property included within the definition of "intangible property" for purposes of tax valuation. Under the repealed Georgia statute subjecting intangible property to an ad valorem tax, the Georgia legislature defined intangible property as:

(1) Money;

(2) Collateral Security Loans;

(3) Stocks;

(4) Accounts receivables and notes not representing credits secured by real estate;

(5) Bonds and debentures of all corporations;

(6) Long term notes secured by real estate;

(7) Short term notes secured by real estate;

(8) Restricted foreign intangibles;

(9) Patents, copyrights, franchises, and all other classes of intangible personal property not otherwise enumerated; and

(10) Computer software defined by statute.

O.C.G.A. § 48-6-21.

Although it has been repealed, O.C.G.A. § 48-6-21 is an indication that the Georgia legislature believed that the assets listed above constitute intangible property. Further, by repealing the statute, the legislature implicitly indicated that these types of intangible property were no longer subject to taxation. The court, therefore, finds that, at the very least, the list of property included in O.C.G.A. § 48-6-21 is a good starting point for defining the term "intangible property."

Despite the repeal of O.C.G.A. § 48-6-21, CSXT claims that its intangible property has been included within the Department's Proposed Valuation. The Department admits that its unit valuation of CSXT initially included CSXT' s [sic] tangible and intangible property, but claims that it deducted $400 million from its unit value to account for CSXT's intangible property.

Instead of attempting to identify and value its intangible property, CSXT contends that it is impractical to identify and value its intangible property, and, thus, the court should require the Department to use the yield capitalization approach, which CSXT contends does not compound intangibles. CSXT claims that the court should require the

defendants to use the yield capitalization approach because the Department's market multiple and stock and debt approaches allegedly unnecessarily compound intangible values.[28] For example, CSXT has presented evidence that a company's stock prices may increase when that company hires a new CEO. This increase in the stock price is not attributable to tangible assets. Because the stock and debt and the market multiple approaches both rely on a company's stock price,[29] they compound intangible assets.

As support for its argument that the court should adopt the yield capitalization approach, CSXT cites to a decision by the Utah Tax Commission ("Commission") in *WilTel, Inc. v. Beaver County*, Nos. 95-0789 and 95-0824 (Utah Tax Commission December 5,, 1997)("*WilTel II*"). WilTel, Inc. is a provider of long-distance telecommunications services. In 1995, the Utah State Property Tax Division (the "Division") calculated WilTel's unit value based on the stock and debt and income approaches. WilTel appealed the assessment to the Utah Tax Commission and moved for partial summary judgment arguing, in part, that Utah's assessment improperly included intangible property, which was not taxable under Utah law. *WilTel, Inc. v. Beaver County*, No. 95-0789, 1997 Utah Tax LEXIS 111, at *2-3 (Utah Tax Commission April 21, 1997) (*"WilTel I"*). The Utah Tax Commission found that the income and stock and debt approaches tend to compound intangible values. The Utah Tax Commission then remanded the case to the parties to identify, value, and re-

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[28] It is undisputed here that the Department does not and did not intend to value the intangible property of other commercial and industrial property. It is also undisputed that all three of the valuation methods used by the Department initially included the value of CSXT's intangible property.

[29] For clarification purposes, unlike the stock and debt approach, the market multiple approach relies on the stock prices of comparable companies, as opposed to CSX Corporation's stock prices.

move WilTel's intangible property using the cost approach." *Id.* at *14-15.

On remand, the parties were unable to agree on the valuation of WilTel's tax-exempt intangible property, and, thus, the matter came before the Utah Tax Commission again for a formal hearing to determine the value of WilTel's intangible property. *WilTel II* at *2. The Commission finally concluded that "separately valuing intangibles and deducting them from a unit valuation is impractical." *WilTel II* at *3. In an attempt to minimize the inclusion of intangibles in the unit rule method, the Utah Tax Commission concluded that the parties should use a yield capitalization approach and a cost approach and that each approach should be weighted at 50%. The Utah Tax Commission then remanded the case to the Division to calculate the value of WilTel under a yield capitalization approach (minus growth) and to time adjust its cost approach. *WilTel II* at *6.

While the *WilTel II* decision is attractive because of its simplicity, the court finds that the reasoning of *WilTel II* is not appropriate in this case. First, this is a case brought under the 4-R Act, and not merely an appeal of a state tax valuation. The court has already held that CSXT may not challenge the Department's valuation methods in this case. If this court were to adopt the reasoning of *WilTel II*, the court would be dictating to the Department a particular valuation method.

Second, CSXT has not convinced the court that it is impossible or impractical to value its intangible property. While CSXT's local assessment expert, Ms. Judith Ross, testified that identifying and valuing a company's intangible property would be extremely difficult, she also testified that performing a unit valuation in general is difficult. Ms. Ross further testified that intangible property can be identified and valued by a person with expertise. Thus, the court finds that it is not impractical or impossible to identify and value CSXT's intangible property.

Third, while the court believes that the stock and debt approach undoubtedly includes value attributable to intangible property in its initial unit value, the court also finds that the yield capitalization method touted by CSXT includes some value attributable to intangible property. In fact, CSXT has admitted that Mr. Tegarden's yield capitalization value includes some value attributable to intangible property. This is further illustrated by the fact that CSXT deducts $400 million from Mr. Tegarden' s unit value of CSXT—the same $400 million deduction that the Department took to account for certain intangibles owned by CSXT.

Fourth, this case differs[30] from the *Wiltel* decisions in that in *Wiltel I,* the Utah Tax Commission remanded the case so that the taxpayer could identify its intangible property. The parties, however, could not agree on the value of Wiltel's intangible property. In this case, CSXT has not even presented any evidence that it owns intangible property.

Here, it is undisputed that Mr. Dickerson deducted $400 million from his unit value of CSXT to account for certain intangibles. He testified that the $400 million deduction was his attempt to eliminate the value of CSXT's intangible property that was previously separately taxed under O.C.G.A. § 48-6-21. When asked why he did not attempt to value and deduct other intangible property from his initial assessment, Mr. Dickerson testified that CSXT did not present the Department with any evidence that CSXT owned other intangible property. Consistent with its statement to Mr. Dickerson, at trial CSXT failed to identify any specific intangible property that it owned as of January 1, 2002.[31] CSXT also failed to

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[30] The court also notes that holdings in the *WilTel* cases are not binding upon this court for numerous reasons: (1) the *Wiltel* decisions were made by the Utah State Tax Commission; (2) the taxpayer in the *Wiltel* cases was a telecommunications company, not a railroad; and (3) the *Wiltel* cases were not decided under the 4-R Act.

[31] For example, CSXT did not provide the court with any evidence that

present evidence as to how much its intangible property was worth. *Cf. Burlington N. R.R. Co. v. Huddleston*, 94 F.3d 1413, 1415 (10th Cir.1996) (in its complaint alleging a violation of the 4-R Act, the railroad also alleged that the value of its intangible property, computer software, was at least $8 million); *Bair*, 815 F.Supp. at 1239 (separately identifying and valuing intangible property of a railroad for purposes of 4-R Act claim). Nor has CSXT provided the court with any evidence that the Department's $400 million intangible property deduction was under-inclusive.

The court, therefore, concludes that CSXT has not carried its burden of showing by a preponderance of evidence that the Department improperly included intangible property in the Department's Proposed Valuation of CSXT.

Conclusion

For the reasons discussed above, the court concludes that the defendants have not discriminated against CSXT in violation of 49 U.S.C. § 11501(b)(4).

The court also holds that the true market unit value of CSXT for the tax year 2002 was $7,726,293,350.[32] The true market value of CSXT's taxable rail transportation property in Georgia for the tax year 2002 was $509,560,171.[33] The defendants, therefore, have not discriminated against CSXT in violation of 49 U.S.C. § 11501(b)(1) because the ratio of assessed value to true market value of CSXT's property does

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it owns any trademarks, copyrights, or patents.

[32] The court arrived at this number by taking the Department's $8,126,293,350 DCF value for CSXT and subtracting $400 million to account for CSXT's intangible property.

[33] The court reached this number by taking the $7,726,293,350 true market unit value of CSXT and allocating 7.194059% to Georgia. The court then deducted $4,156,193 to account for CSXT's motor vehicles, $2,907,467 to account for pollution control, and $39,210,271 to account for W & A exempt line.

not exceed the jurisdictional threshold set out in the 4-R Act of 42%. Thus, CSXT is not entitled to relief under the 4-R Act for the tax year 2002.

The clerk is DIRECTED to close this file and issue judgment for the defendants in accordance with this order.

APPENDIX C

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

[Filed FEB 12, 2007]

No. 05-16000-CC

CSX TRANSPORTATION, INC.,
Plaintiff-Appellant,

versus

STATE BOARD OF EQUALIZATION, of the State of Georgia, JERRY JACKSON, as Commissioner of Revenue of the State of Georgia, RUSSELL W. HINTON, as State Auditor of the State of Georgia, RAY J. CRAWFORD, as Director of the Georgia State Properties Commission,
Defendants-Appellees.

On Appeal from the United States District Court
for the Northern District of Georgia

ON PETITION(S) FOR REHEARING AND PETITION(S)
FOR REHEARING EN BANC

Before: BIRCH, PRYOR and FAY, *Circuit Judges.*

PER CURIAM:

The Petition(s) for Rehearing are DENIED and no Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure), the Petition(s) for Rehearing En Banc are DENIED.

ENTERED FOR THE COURT:

/s/ [Illegible]
UNITED STATES CIRCUIT JUDGE

APPENDIX D

FEDERAL STATUTE

49 U.S.C. § 11501 (2002) Tax discrimination against rail transportation propery

(a) In this section—

(1) the term "assessment" means valuation for a property tax levied by a taxing district;

(2) the term "assessment jurisdiction" means a geographical area in a State used in determining the assessed value of property for ad valorem taxation;

(3) the term "rail transportation property" means property, as defined by the Board, owned or used by a rail carrier providing transportation subject to the jurisdiction of the Board under this part; and

(4) the term "commercial and industrial property" means property, other than transportation property and land used primarily for agricultural purposes or timber growing, devoted to a commercial or industrial use and subject to a property tax levy.

(b) The following acts unreasonably burden and discriminate against interstate commerce, and a State, subdivision of a State, or authority acting for a State or subdivision of a State may not do any of them:

(1) Assess rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.

(2) Levy or collect a tax on an assessment that may not be made under paragraph (1) of this subsection.

(3) Levy or collect an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.

(4) Impose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the Board under this part.

(c) Notwithstanding section 1341 of title 28 and without regard to the amount in controversy or citizenship of the parties, a district court of the United States has jurisdiction, concurrent with other jurisdiction of courts of the United States and the States, to prevent a violation of subsection (b) of this section. Relief may be granted under this subsection only if the ratio of assessed value to true market value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction. The burden of proof in determining assessed value and true market value is governed by State law. If the ratio of the assessed value of other commercial and industrial property in the assessment jurisdiction to the true market value of all other commercial and industrial property cannot be determined to the satisfaction of the district court through the random-sampling method known as a sales assessment ratio study (to be carried out under statistical principles applicable to such a study), the court shall find, as a violation of this section—

(1) an assessment of the rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the assessed value of all other property subject to a property tax levy in the assessment jurisdiction has to the true market value of all other commercial and industrial property; and

(2) the collection of an ad valorem property tax on the rail transportation property at a tax rate that exceeds the tax ratio rate applicable to taxable property in the taxing district.

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(2)

No. 06-1287

FILED

APR 23 2007

OFFICE OF THE CLERK
SUPREME COURT, U.S.

In The

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA; BART L. GRAHAM, AS COMMISSIONER OF REVENUE OF THE STATE OF GEORGIA; RUSSELL W. HINTON, AS STATE AUDITOR OF THE STATE OF GEORGIA; AND GENA L. ABRAHAM, AS DIRECTOR OF THE GEORGIA STATE PROPERTIES COMMISSION,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Eleventh Circuit

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

PETER J. CROSSETT
JOHN D. COOK
HISCOCK & BARCLAY, LLP
One Park Place
300 South State Street
Syracuse, New York
13202-2078
(315) 425-2814

WARREN R. CALVERT
Senior Assistant Attorney General
(*Counsel of Record for Respondents*)

THURBERT E. BAKER
Attorney General

R. O. LERER
Deputy Attorney General

GEORGIA DEPARTMENT OF LAW
40 Capitol Square, S.W.
Atlanta, Georgia 30334-1300
(404) 656-2647

Attorneys for Respondents

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTION PRESENTED FOR REVIEW

Whether a railroad may, in an action under 49 U.S.C. § 11501(b)(1) claiming that the State has overvalued the railroad's transportation property for tax purposes, challenge the appropriateness of the methods by which the State determined such property's true market value or is instead restricted to challenging the factual determinations to which the State's methods were applied.

PARTIES TO THE PROCEEDINGS

The parties before the Eleventh Circuit Court of Appeals included Georgia's State Revenue Commissioner and the Director of the Georgia State Properties Commission in their official capacities. While this litigation was pending in the district court Bart L. Graham succeeded T. Jerry Jackson as State Revenue Commissioner and was automatically substituted as a party pursuant to Fed. R. Civ. P. 25(d)(1). Ray J. Crawford passed away after CSX Transportation, Inc. filed its notice of appeal to the circuit court, and Gena L. Abraham was appointed to replace him as director of the Georgia State Properties Commission prior to the Eleventh Circuit's decision, resulting in her automatic substitution as a party pursuant to Fed. R. App. P. 43(c)(2).

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STATEMENT OF THE CASE

I. Nature Of The Litigation And Question Presented

Petitioner CSX Transportation, Inc. ("CSXT"), an interstate common carrier by rail, filed the instant action in September 2002 against the Georgia State Board of Equalization and its individual members, including the State Revenue Commissioner,[1] challenging the State's proposed assessment of the railroad's operating property for 2002 ad valorem tax purposes under Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, 90 Stat. 54 (Feb. 5, 1976) ("the 4-R Act"), currently codified at 49 U.S.C. § 11501 ("Section 11501"). CSXT contended that the State's proposed assessment violated Section 11501(b)(1), which prohibits

> assess[ing] rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.

Pet. App. 75a. More specifically, CSXT argued that the State had significantly overvalued the railroad's transportation property, resulting in a ratio of assessed value to true market value for that property of approximately 55%, while other commercial and industrial property was assessed at only 40% of its value. Complaint, ¶¶ 21, 24.

In *Burlington Northern Railroad Co. v. Oklahoma Tax Comm'n*, 481 U.S. 454 (1987) ("*Oklahoma Tax*"), this Court

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[1] For simplicity purposes, the Respondents will also be referred to collectively as "the State."

held that Section 11501[2] permitted review by federal courts of alleged overvaluation of railroad properties by state tax authorities. The Tenth Circuit had upheld the dismissal of a railroad's complaint on the ground that a preliminary showing of intentional discrimination was required before such a claim could be considered. *See Burlington N. R.R. Co. v. Okla. Tax Comm'n*, 1986 U.S. App. LEXIS 36936 (10th Cir. May 2, 1986). *See also Oklahoma Tax*, 481 U.S. at 460-61. Oklahoma's taxing officials suggested to this Court "that [Section 11501] *never* permits district court review of such claims." *Id.* at 461 (emphasis in original). The Court rejected both positions. *Id.*

But the Court expressly left open the legal question presented here. Oklahoma's tax officials had derived the railroad's value by taking a weighted average of original cost and capitalized net operating income. *Oklahoma Tax*, 481 U.S. at 459. Although it ruled for the railroad, the Court noted that:

> Petitioner has not challenged the valuation *methodology* employed by respondents in determining the value of petitioner's railroad; petitioner's sole challenge is to the *application of that methodology*, particularly the State's evaluation of the cost of capital and the State's refusal to make deductions for property which petitioner claims is obsolete. Tr. Of Oral Arg. 15-16. This case therefore does not present the question of whether a railroad may, in an action under [Section 11501], challenge in the district court the

[2] At the time *Oklahoma Tax* was decided Section 11501 was codified as 49 U.S.C. § 11503.

> appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied. Accordingly we express no view on that issue.

Oklahoma Tax, 481 U.S. at 463 n.5 (emphasis added). In this case the courts below decided that question in the State's favor.

II. The "True Market Value" Of CSXT's Transportation Property In Georgia

A. *The State's Proposed Assessment.* The Georgia Department of Revenue annually prepares a proposed assessment of CSXT's operating properties for each Georgia county in which the railroad has taxable property. Pet. App. 2a, 3a, 30a. In valuing CSXT's operating property for 2002 ad valorem tax purposes, the State used the unit rule, which the parties in this case agree is appropriate under Georgia law. Pet. App. 3a, 30a, 31a. Under the unit rule, the State first determined the value of the railroad as an entire operating system irrespective of where the operating property was located and without functional or geographic division of the whole into its component parts. *Id.*

The State's proposed assessment was based on an $8.2 billion unit value estimate for CSXT, from which $400 million was deducted to eliminate the effect of certain intangible assets. Pet. App. 5a, 32a. The adjusted unit value of $7.8 billion then was allocated to Georgia using the percentage of Georgia road miles to system road miles, resulting in an allocated value of $561,136,602. *Id.* To arrive at CSXT's Georgia taxable fair market value – $514,862,672 – the State deducted amounts for motor

vehicles (which are separately valued and assessed for ad valorem tax purposes), exempt pollution control equipment, and an exempt railroad line. *Id.* CSXT does not dispute the $400 million adjustment, the track-mile allocation percentage, or the deductions for motor vehicles, exempt pollution control equipment, and exempt line. *Id.* at 7a. Rather, CSXT contends that the railroad's system wide unit value was only $6 billion, resulting in a Georgia taxable fair market value of just $369,253,752. *Id.* at 7a, 36a.

Mr. Gregg Dickerson, the Revenue Department's Public Utility Manager, prepared the State's proposed assessment. Mr. Dickerson had worked at the Department of Revenue for approximately ten years preparing public utility valuations before leaving in 1993 to take a position in the tax department at Norfolk Southern Railroad. Pet. App. 3a, 4a, 31a. When Mr. Dickerson returned to government service in 2001 the State was calculating unit values using a yield capitalization method, a direct capitalization method, and a stock-and-debt method. *Id.* at 4a. For the tax year 2002, Mr. Dickerson replaced the first two methodologies with discounted cash flow ("DCF") and market multiples methods, but he kept the stock-and-debt method. *Id.*

Importantly, Mr. Dickerson also instituted a change in 2002 for railroads that was not needed for other public utilities: he began to use income figures taken from the companies' annual reports to shareholders instead of their regulatory reports to the Surface Transportation Board ("R-1 reports") to project future cash flows in his DCF analysis. Pet. App. 63a. As he explained at trial:

> [T]he state of Georgia, like most states, have [sic] historically relied on regulatory reports as our sources of income information and cost information. I found out . . . while working at Norfolk Southern that investors in the railroad . . . rarely even know what an R-1 is. It's not something that they look at in determining their analysis of a railroad company. They look at the annual reports to stockholders, the 10K's filed with the [SEC]. That was the type of information they were interested in, and . . . to replicate the actions of the market [in valuing the railroad], I thought they were a better source of income information.

Tr., Vol. 5, p. 774. CSX Corporation's Vice President and Controller acknowledged at trial that management's view of the railroad's financial performance was reflected in the annual report figures and not the R-1's. Pet. App. 63a; Tr., Vol. 6, pp. 886-88, 892. The figures in these reports can vary greatly,[3] and the largest part of the 47% increase in CSXT's 2002 assessment over 2001 was due to that change in the income amounts used to value the company. Pet. App. 63a.

Mr. Dickerson's DCF analysis yielded a 2002 unit value of $8.126 billion. Pet. App. 4a, 5a, 31a, 32a. His stock-and-debt method showed a unit value of $12.022 billion. *Id.* at 4a, 31a, 32a. Mr. Dickerson derived three indicators of CSXT's unit value using the market multiples

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[3] For example, CSX Corporation's annual report for 2001 showed that its rail segment had operating income of $743 million, but CSXT's R-1 report to the Surface Transportation Board reflected "net railroad operating income" of only $458 million for the same period. Tr., Vol. 5, pp. 776-78.

method, which yielded values of $12.346 billion, $10.769 billion, and $8.474 billion. *Id.* at 5a, 31a, 32a. Mr. Dickerson concluded that a unit value of $8.2 billion was at the lower end of the range within which CSXT's true value would lie, and he chose that value in order to be conservative and avoid litigation if possible. *Id.* at 5a; Tr., Vol. 2, pp. 215, 310, 326-27.

B. *CSXT's Appraisal.* CSXT relied on an appraisal by Mr. Thomas Tegarden in arguing that the State had significantly overstated the railroad's unit value for the 2002 tax year. Mr. Tegarden derived unit value estimates of $9.637 billion, $5.983 billion, and $6.15 billion using, respectively, a stock-and-debt method, a yield capitalization method, and a cost method. Pet. App. 41a. He gave no weight to the stock-and-debt method and little weight to his cost method in concluding that CSXT's unit value was only $6 billion. *Id.* at 7a, 36a, 41a.

III. The Rulings By The Courts Below

A. *The District Court.* Agreeing with the Fourth Circuit's decision in *Chesapeake Western Railway v. Forst*, 938 F.2d 528 (4th Cir. 1991), *cert. denied*, 503 U.S. 966 (1992) ("*Chesapeake Western*"), the district court held that it "[could not] consider Mr. Tegarden's valuation because it was prepared using different valuation methods than the Department." Pet. App. 37a n.8.[4] The court then carefully

[4] Nevertheless, the court expressed serious reservations about the unit value estimate of CSXT's appraiser, as it failed at least one straightforward test of reasonableness. "If, as CSXT claims, the value of CSXT was $6 billion, CSXT would have a negative equity value. CSX Corporation [the railroad's parent], however, held investment grade bond ratings implying a profitability level in excess of that needed to

(Continued on following page)

analyzed and rejected each of CSXT's myriad objections to the State's application of the DCF methodology, including the company's assertion that a 69% increase in free cash flow from 2001 to 2002 was "bizarre," that the railroad could not be expected to achieve an 80% operating ratio by the year 2011, that a 6.3% terminal growth rate was unrealistic, and that a "leased equipment" adjustment to the unit value was inappropriate. Pet. App. 48a-51a, 56a-59a.

The district court recognized that it had to "weigh the evidence and make its own factual findings regarding the true market value of CSXT." Pet. App. 44a. That process was succinctly described by the court as follows:

> After parsing through days of expert testimony, the court concludes that the Department's DCF value as set out in its Proposed Valuation is the most accurate indicator of CSXT's unit value. As a result, the court holds that, for purposes of applying the 4-R Act to the defendants' assessments of CSXT, the true market unit value of CSXT for the tax year 2002 was $7,726,293,350.

Pet. App. 59a.[5] Using the State's track-mile allocation percentage and deductions for motor vehicles and certain exempt property, the court found that "[t]he true market value of CSXT's taxable rail transportation property in Georgia for the tax year 2002 . . . was $509,560,171" and

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pay both current interest expenses and the principal balance of debt." Pet. App. 53a n.12.

[5] "The court arrived at this number by taking the Department's $8,126,293,350 DCF value for CSXT and subtracting $400 million to account for CSXT's intangible property." Pet. App. 59a n.23.

that there was no violation of Section 11501(b)(1). Pet. App. 59a-60a.

B. *The Eleventh Circuit's Decision.* The Eleventh Circuit affirmed the district court in a 2-1 decision. The Eleventh Circuit agreed with the district court and *Chesapeake Western* "that railroads may not challenge state valuation methodologies under subsection (b)(1) [of Section 11501]." Pet. App. 14a. The Eleventh Circuit recognized that a state's taxation authority is central to state sovereignty. Pet. App. 12a. *See also Department of Revenue v. ACF Indus.*, 510 U.S. 332, 345 (1994) ("*ACF Industries*"); *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110 (1871) ("*Dows*") ("[i]t is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments"). The court also noted that "[t]he selection of a valuation methodology is part of this fundamental power of a state," Pet. App. 12a, and that long recognized "principles of federalism and comity generally counsel that courts should adopt a hands-off approach with respect to state tax administration," Pet. App. 12a-13a (quoting *National Private Truck Council v. Okla. Tax Comm'n*, 515 U.S. 582, 586 (1995) ("*National Private Truck Council*")). Accordingly, "a statute will not be construed to burden states in the exercise of their traditional powers unless it clearly states its intent to do so." Pet. App. 11a.

In the Eleventh Circuit's view, "[t]he text of [Section 11501] does not clearly state that railroads may challenge valuation methodologies. Without that clear statement of congressional intent, the argument of the Railroad fails." Pet. App. 14a. The court also looked to the statute's legislative history. The committee report on Senate Bill 927 (involving a precursor to Section 11501) provided that:

> *[the bill] does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves.* It merely provides a single standard against which all affected assessments must be measured in order to determine their relationship to each other. It is not a standard for determining value; it is a standard to which values that have already been determined must be compared.

S. Rep. No. 1483, 90th Cong., 2d Sess. App. B, p. 22 (1968) (emphasis added). *See also* Pet. App. 14a; *Chesapeake Western*, 938 F.2d at 531. A railroad representative who testified during hearings on another earlier version of Section 11501 stated that "[t]he standards and methods of valuation that any State wishes to use would be unaffected by this legislation." *Hearing Before the Subcommittee on Transportation and Aeronautics of the Committee on Interstate and Foreign Commerce on H.R. 16245*, 91st Cong., 1st Sess. 138 (1970) (testimony of Philip M. Lanier). Pet. App. 14a. The Eleventh Circuit therefore found that "[t]he legislative history . . . supports the conclusion that railroads may not challenge state valuation methodologies in federal court." *Id.* at 14a. The Eleventh Circuit also upheld the district court's finding "that the appraisal prepared for the Railroad by Tegarden was based on a methodology different from the methodology used by the State." *Id.* at 17a.

The dissent agreed that there was no merit to the railroad's argument that its appraiser used the same methodology as the State. However, the dissent felt that Section 11501 permitted a railroad to challenge the State's methodology. *Id.* at 20a-23a. CSXT's petition for rehearing en banc was denied. *Id.* at 73a.

REASONS FOR DENYING THE PETITION

I. The Two Circuits That Have Addressed The Issue In Reviewing Final Decisions On The Merits Have Held That A Railroad May Not Challenge A State's Chosen Valuation Methodology Under 49 U.S.C. § 11501(b)(1)

CSXT asserts that there is now a "mature" 2-2 split between the Second and Ninth Circuits on the one hand, and the Fourth and Eleventh Circuits on the other, regarding the question left open in *Oklahoma Tax*, and that the divergence requires intervention by this Court. In fact, the Fourth and Eleventh Circuits are the only federal courts of appeal to have considered this issue in reviewing final decisions on the merits, and both courts have held that a railroad – although it may dispute the way in which a state applied a particular valuation methodology – cannot challenge the methodology itself. The Second Circuit has stated otherwise in a case that involved only the grant of a preliminary injunction, where the standard was whether "reasonable cause" existed to believe that a violation of the 4-R Act was about to occur, and where that test was met even when using the state's own value for the railroad property. The Ninth Circuit has yet to squarely address the issue. Respondents respectfully submit that a grant of certiorari is not warranted under these circumstances. The Second, Fourth, and Ninth Circuit cases are discussed below.

A. *The Fourth Circuit.* In *Chesapeake Western*, the Fourth Circuit considered the question left open in *Oklahoma Tax* and held that Section 11501 does not provide a basis for parties to challenge a state's chosen valuation methods:

> As an initial matter, we note that Congress has enacted a general proscription on federal interference in state taxation decisions. *See* 28 U.S.C. § 1341[6]; *Burlington Northern R.R. v. Lennen*, 715 F.2d 494, 498 (10th Cir. 1983). While [Section 11501] was passed as an express exception to the policy of non-interference, *id.*, we are not inclined to disregard this general policy in areas where [Section 11501] does not plainly authorize such an exception and where the federal courts are ill equipped to evaluate the merits of a challenge to a state taxation scheme. . . .
>
> The Supreme Court has held that [Section 11501] unambiguously provides a basis for railroads to challenge a state's calculation of the true market value of railroad property under whatever accounting system prevails in a given state. *Burlington Northern R.R. v. Oklahoma Tax Comm'n*, 481 U.S. at 461-63, 107 S.Ct. at 1859-61. On the other hand, the statute is not so explicit in explaining whether a railroad may challenge, in addition, the particular accounting method a state has determined to best estimate true market value. Since the statute is ambiguous on this latter question, we turn to the legislative history of [Section 11501].

Chesapeake Western, 938 F.2d at 531. The Fourth Circuit noted that "the history that does exist suggests that Congress did not intend for courts to displace the state's

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[6] The Tax Injunction Act, 28 U.S.C. § 1341, bars federal jurisdiction when the relief requested by the plaintiff would "enjoin, suspend, or restrain" the assessment, levy or collection of any tax under State law and the State affords a "plain, speedy and efficient remedy." *See also Fair Assessment in Real Estate Ass'n v. McNary*, 454 U.S. 100 (1981) (principle of comity acts as similar bar).

policy choice about what constitutes the best method for determining true market value of railroad land." *Id.*

The Fourth Circuit also recognized that "[t]he job of determining whether a particular valuation method produces a 'true' market value involves, at its core, a policy choice. The concept of true market value is inherently an approximation, in some sense a fiction, since there is no such thing as a perfect market." *Chesapeake Western*, 938 F.2d at 531. As explained by the district court in *Union Pacific Railroad Company v. State Tax Commission*, 716 F. Supp. 543 (D. Utah 1988), whose reasoning the Fourth Circuit embraced:

> The plaintiffs argue . . . that the statute itself requires this court to choose the correct valuation method from among the competing methods. They argue that the statute requires the court to determine their "true market value" and that the only way the court can do that is by determining which method gives the "true" true market value. That method is the one that is most reasonable and most accurate and hence arrives at the most correct result.
>
> . . .
>
> Each expert asserts that his methodology results in a value that most closely responds to reality. However, absent a willing buyer and a willing seller, there is no absolute way to test the assertions of competing valuations or competing claims of correspondence to "true market value," if such a thing exists in the order of things.

Id. at 553. The Fourth Circuit described valuation as "an art, not a science," "a function of judgment, not of natural law," and said that "it is clear that there is more than one

way to value a railroad." *Chesapeake Western*, 938 F.2d at 532 (quoting *Union Pacific*, 716 F. Supp. at 554-55). Under these circumstances, "the railroads could not establish that their proposed methodology was, in some absolute sense, 'truer' than any other." *Chesapeake Western*, 938 F.2d at 532.

CSXT argued in the court below that the Fourth Circuit "partially retreated" from its holding in *Chesapeake Western* when it later decided *Richmond, Fredericksburg & Potomac Railroad Co. v. Forst*, 4 F.3d 244 (4th Cir. 1993) ("*RF&P*"). CSXT C.A. Br. at 37. CSXT now concedes that *RF&P* reaffirmed *Chesapeake Western*, Pet., p. 14, and that the rule is firmly established in the Fourth Circuit that "[Section 11501(b)(1)] does not provide a basis for railroads to challenge a state's preferred methodology for ascertaining the true market value of railroad property." *RF&P*, 4 F.3d at 248. "[A] railroad may present independent evidence of the fair market value of its property, provided . . . that it limits its evidence to factors that may properly be taken into account under the state's chosen methodology." *Id.* at 250.

B. *The Second Circuit.* In contrast to the Fourth Circuit's holding in *Chesapeake Western* and the opinion of the Eleventh Circuit in this case, the Second Circuit's decision in *Consolidated Rail Corp. v. Town of Hyde Park*, 47 F.3d 473 (2d Cir. 1995) ("*Conrail*") involved an appeal from the district court's grant of a preliminary injunction in favor of the railroad rather than a final decision on the merits. The Second Circuit began by stating that "[f]or such a statutory injunction, a railroad need only demonstrate that there is 'reasonable cause' to believe that a violation of the 4-R Act has occurred or is about to occur." *Id.* at 479. *Cf. Johnson & Johnson Vision Care, Inc. v.*

1-800 Contacts, Inc., 299 F.3d 1242, 1246 (11th Cir. 2002) (normally "the movant [for a preliminary injunction] must establish . . . a substantial likelihood of success on the merits"). There was no question in *Conrail* that "reasonable cause" had been shown, since "even if the defendants' true market value of $974 million is accepted, the resulting [assessment] ratio for Conrail would be 63% . . . and this too would be a violation of the 4-R Act." *Conrail*, 47 F.3d at 480. In other words, because the state's application of its own methodology resulted in a 4-R Act violation, injunctive relief clearly was appropriate. Furthermore, unlike the careful, detailed discussions of the "methodology" issue set forth in *Chesapeake Western* and the court below, that portion of the Second Circuit's opinion is a mere six sentences, which consist mainly of stating the question and the court's conclusion. *See id.* at 481-82. The court also seemed most influenced by the fact that New York had adopted what the Second Circuit characterized as "a special appraisal method for railroads alone" that would circumvent "the whole nondiscrimination objective of the statute."[7] *Id.* The parties eventually settled, prior to a final decision on the merits. *CSX Transp., Inc. v. New York State Office of Real Property Servs.*, 306 F.3d 87, 90-91 (2d Cir. 2002).

C. *The Ninth Circuit.* The Ninth Circuit's opinion in *Burlington Northern Railroad Co. v. Department of Revenue*, 23 F.3d 239 (9th Cir. 1994), affirmed a district

[7] Ironically, a "special appraisal method" is precisely what CSXT wants in this case. The district court found – and CSXT does not dispute here – that the State valued CSXT essentially the same way that it valued every public utility appraised under the unit rule. Pet. App. 62a.

court decision that largely upheld the State of Washington's valuation of a railroad's transportation assets.[8] On appeal, the railroad asserted that "in deferring to the state's choice of the valuation method used to set the market value of its property" the district court had wrongly relied on the Fourth Circuit's *Chesapeake Western* decision. But the Ninth Circuit stated that:

> *[w]e need not decide whether Chesapeake Western should be followed in this circuit.* Here, the district court cited *Chesapeake Western*, but it did not preclude Burlington Northern from challenging the state's method of valuation. The court allowed Burlington Northern to present evidence of the railroad's value based on other valuation methods.

Id. at 240-41 (emphasis added). Respondents respectfully submit that the circuit court below misapprehended the basis of the Ninth Circuit's decision, which it characterized as having "repudiated *Chesapeake Western*," Pet. App. 10a, and that the Ninth Circuit has not yet squarely addressed the question presented here.

However, the Ninth Circuit did squarely reject the railroad's assertion that the district court erred in attributing to the state's valuation a presumption of correctness that had to be defeated by "clear, cogent and convincing" evidence. *Id.* at 241. The court disagreed with the railroad that affording "substantial deference" to the state's valuation method violated the railroad's alleged right under the 4-R Act to establish the correct value "by any appropriate

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[8] The district court made only two adjustments to the state's value. *Id.* at 240.

valuation approach." *Id.* Notably, this is the same right claimed by CSXT here. Pet., p. 17 (stating that fair market value must be decided "based on *all* relevant evidence") (emphasis added); *id.* at 19 ("Section 11501 requires courts to determine the 'true market value' of railroad property based upon *any and all* competent evidence.") (emphasis added).

II. The Eleventh Circuit's Decision Is Correct

CSXT contends that "this Court's intervention is all the more imperative given the Eleventh Circuit's critical error in interpreting Section 11501." Pet., p. 16. However, the railroad's petition does not dispute much of the legal basis for the Eleventh Circuit's decision, *e.g.*, that a state's taxation authority is central to state sovereignty, Pet. App. 12a; *see also ACF Industries*, 510 U.S. at 345; *Dows*, 78 U.S. (11 Wall.) at 110 ("[i]t is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments"); that "[t]he selection of a valuation methodology is part of this fundamental power of a state," Pet. App. 12a; and that "principles of federalism and comity generally counsel that courts should adopt a hands-off approach with respect to state tax administration," Pet. App. 12a-13a (quoting *National Private Truck Council*, 515 U.S. at 586).

Nor does CSXT take issue with the well-established principle of statutory interpretation that the Eleventh Circuit applied in ruling for the State. As this Court pointed out in *Atascadero State Hospital v. Scanlon*, 473 U.S. 234, 242 (1985) ("*Atascadero*"), if Congress means to alter the "usual constitutional balance between the States

and the Federal Government" it must make that intention "unmistakably clear in the language of the statute." *Atascadero* went on to hold that States were not subject to suit in federal court by litigants seeking retroactive monetary relief under a statute providing that its remedies "shall be available to any person aggrieved by any act or failure to act by any recipient of Federal assistance" and where the State of California received such federal aid. *Id.* at 245-46. According to the Court, the statute failed to unequivocally express Congress' intent to abrogate the Eleventh Amendment bar to suits against the States in federal court. *Id.*

The "plain statement rule" has been described as "an acknowledgment that the States retain substantial sovereign powers under our constitutional scheme, powers with which Congress does not readily interfere." *Gregory v. Ashcroft*, 501 U.S. 452, 461 (1991) ("*Gregory*"). For that reason, although "*Atascadero* was an Eleventh Amendment case, . . . a similar approach is applied in other contexts." *Will v. Mich. Dep't of State Police*, 491 U.S. 58, 65 (1989). The Court used this rule of statutory construction in *Gregory* to hold that Missouri's mandatory retirement requirement for judges did not violate the federal Age Discrimination in Employment Act of 1967 ("ADEA"). The Court observed that "[t]he present case concerns a state constitutional provision through which the people of Missouri establish a qualification for those who sit as their judges. This . . . is a decision of the fundamental sort for a sovereign entity." *Gregory*, 501 U.S. at 460. The ADEA plainly applied to States as employers, *id.* at 464, but the Court would "not read the ADEA to cover state judges

unless Congress has made it clear that judges are included. This does not mean that the Act must mention judges explicitly, though it does not. [Citation omitted.] Rather it must be plain to anyone reading that Act that it covers judges." *Id.* at 467 (emphasis omitted).

Most importantly, this Court has recognized that the same rule of construction applies in interpreting Section 11501. In *ACF Industries*, the Court held that Section 11501(b)(4) – which prohibits the imposition of "another tax that discriminates against a rail carrier providing transportation" – does not limit a State's discretion to exempt non-railroad property from generally applicable ad valorem property taxes.

> Principles of federalism support, in fact compel, our view. [Section 11501] sets limits upon the taxation authority of state government, an authority we have recognized as central to state sovereignty. When determining the breadth of a federal statute that impinges upon or pre-empts the States' traditional powers, we are hesitant to extend the statute beyond its evident scope. We will interpret a statute to pre-empt the traditional state powers only if that result is "the clear and manifest purpose of Congress." As explained above, neither [the particular subsection] nor the whole of [Section 11501] meets this standard with regard to the prohibition of property tax exemptions.

ACF Industries, 510 U.S. at 345 (internal citations omitted).

Although *Oklahoma Tax* held that the express language of Section 11501(b)(1) plainly allows a railroad to

litigate the value placed by the state on the railroad's transportation property, the text does not clearly state that railroads may challenge both the way in which the state has applied a particular valuation method and the method itself, and the Eleventh Circuit properly refused "to extend the statute beyond its evident scope." That holding is supported by the 4-R Act's legislative history, to which this Court itself referred in *ACF Industries*, noting that:

> [the taxpayers could not] draw our attention to a single instance in the 15-year legislative history of the 4-R Act in which representatives of the railroad industry expressed concern about discriminatory property tax exemptions. In fact, when urging the Senate to adopt [that portion of Section 11501], industry representatives characterized the provision as prohibiting only discriminatory in lieu taxes and gross receipts taxes; property tax exemptions, in contrast, were not mentioned.

ACF Industries, 510 U.S. at 346. Section 11501's legislative history is similarly revealing on the question presented here. An industry representative who testified during committee hearings stated that "[t]he standards and methods of valuation that any State wishes to use would be unaffected by this legislation." *Hearing Before the Subcommittee on Transportation and Aeronautics of the Committee on Interstate and Foreign Commerce on H.R. 16245*, 91st Cong., 1st Sess. 138 (1970)) (testimony of Philip M. Lanier). A committee report also stated that "[the bill] does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves." S. Rep. No. 1483, 90th Cong., 2d

Sess. App. B, p. 22 (1968). While not extensive, this background fully supports the Eleventh Circuit's decision.

CSXT has asserted that the ruling below deprives a railroad of any meaningful opportunity to litigate its fair market value in a lawsuit under Section 11501(b)(1). The trial in this case belies such hyperbole. During the eight days of testimony, not a single witness – with the exception of Mr. Tegarden himself – spoke at any length in support of the railroad's appraisal. Instead, CSXT focused its time and considerable resources, including five expert witnesses, on attacking the State's appraiser and the way he applied the State's valuation methodologies. The company challenged the "comparability" of the Class I railroads that Mr. Dickerson selected to estimate CSXT's unit value under the "market multiples" method; his stock-and-debt method; virtually every assumption made by Mr. Dickerson in applying the DCF method, including the terminal growth rate and projected operating ratio in year 2011; and Mr. Dickerson's "leased equipment" adjustment. Pet. App. 47a-59a. There is no merit to CSXT's claim that the district court effectively denied the railroad a chance to litigate its fair market value; the court simply refused to substitute CSXT's valuation method for the State's, and it methodically rejected the company's criticisms regarding the State's application of the DCF. The Eleventh Circuit's decision allows railroads wide latitude to show that a state has miscalculated the "true market value" of their transportation property, without extending Section 11501 into matters of state tax administration that are beyond the statute's "evident scope."

III. CSXT's Allegations Of "Recent Rapid And Aggressive Escalation Of State Property Valuations" That It Attributes To The Holdings Of The District Court And Eleventh Circuit In This Case Are Unsupported By The Record

Finally, CSXT attempts to attribute an improper "escalation of [its] state property valuations" to the holdings of the district court and Eleventh Circuit in this case, asserting that "there is already evidence that state appraisers are becoming bolder in their determinations of 'true market value' for railroads running through their States" and that this Court must act to "rectify the state methodology abuses that are currently [being] practiced." Pet., pp. 19, 20, 22. CSXT points to its 2006 property tax assessments in Georgia and Florida and claims that both states "adopted CSXT unit values . . . which far exceeded the average value . . . in the other States in the Fourth and Eleventh Circuits that use the unit value method." Pet., p. 22.

Nothing concerning CSXT's 2006 property tax situation – whether in Georgia, Florida, or any other state – is part of the record in this case. CSXT's complaints in this regard therefore should just be ignored. *See generally Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503, 518 n.22 (1981) ("Because these additional facts are not part of the record before us, we have not considered them.") Furthermore, while this Court ordinarily presumes that public officials have "properly discharged their official duties," *Bracy v. Gramley*, 520 U.S. 899, 909 (1997) (quoting *United States v. Chemical Found., Inc.*, 272 U.S. 1, 14-15 (1926)), CSXT takes a virtually opposite view. The company complains of "self-interested valuation methods employed by state tax agencies," insisting that it has been

the victim of an "aggressive and discriminatory escalation of railroad valuations and tax burdens," simply by pointing to tax increases from one year to the next in a particular state or comparing one state's unit value for the company to another's.[9] Pet., p. 22. As the Ninth Circuit observed in *Burlington Northern Railroad Co. v. Department of Revenue*, 23 F.3d at 241, in affirming the district court's refusal to admit evidence of other states' valuations in a Section 11501 challenge:

> Some of the figures reflecting the valuations other states had placed on Burlington Northern's nationwide transportation property resulted from negotiations between Burlington Northern and various state officials. These figures represented compromise values which, as the district court noted, would be only marginally relevant to show that Washington's valuation of Burlington Northern's nationwide property was incorrect. Moreover, had the district court admitted some or all of these figures into evidence, the state most certainly would have sought to examine witnesses to ascertain just how the various other states' valuations were determined. Such a challenge would have extended the trial by a considerable period without appreciable benefit.

What the record in this case does show, however, is a situation where a large tax increase was warranted. Throughout this litigation CSXT has tried to make much of the fact that from 2001 to 2002 its Georgia property tax

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[9] It is noteworthy that even under CSXT's view of Section 11501's scope, federal judges in the states where the company might challenge its property tax valuations could find different unit values for the same tax year.

assessment went up significantly. *See, e.g.*, Pet., p. 7 ("The appraiser's 2002 overall unit value for CSXT of $8.2 billion was 47.1% higher than the 2001 valuation."); *id.* at 20 ("the 2002 Georgia taxable value for CSXT was $514.9 million, 36.3% higher than the 2001 value.") But the district court correctly observed that:

> [t]he fact that [the railroad's] 2002 assessment was 47.1% higher than its 2001 assessment, and that this percentage increase is much higher than the percentage increase of other centrally-assessed taxpayers, does not in and of itself show that CSXT has been discriminated against. An equally likely proposition is that CSXT was undervalued in 2001.

Pet. App. 62a. The State's appraiser also testified that the largest part of the increase in CSXT's 2002 assessment was due to his use that year of income figures taken from the annual reports to shareholders instead of R-1 reports to the Surface Transportation Board to project future cash flows in his discounted cash flow analysis. Pet. App. 63a. That change essentially was endorsed by CSX Corporation's own Vice President and Controller, who acknowledged at trial that management's view of the railroad's financial performance was reflected in the annual report figures and not the regulatory reports. Pet. App. 63a; Tr., Vol. 6, pp. 886-88, 892.

In addition, the State's appraiser selected a unit value that was at the lower end of the range within which CSXT's true value would lie in order to be conservative and avoid litigation if possible. Pet. App. 5a; Tr., Vol. 2, pp. 215, 310, 326-27. The record in this case reflects a conscientious effort by state officials to arrive at a reasonable assessment, not the adoption of what CSXT considers a

"breathtakingly high unit value" designed to extract from the railroad more than its fair share of property taxes.

CONCLUSION

For the reasons above, the Respondents respectfully submit that the petition for writ of certiorari should be denied.

Respectfully submitted,

PETER J. CROSSETT
JOHN D. COOK
HISCOCK & BARCLAY, LLP
One Park Place
300 South State Street
Syracuse, New York
13202-2078
(315) 425-2814

WARREN R. CALVERT
Senior Assistant Attorney General
(Counsel of Record for Respondents)

THURBERT E. BAKER
Attorney General

R. O. LERER
Deputy Attorney General

GEORGIA DEPARTMENT OF LAW
40 Capitol Square, S.W.
Atlanta, Georgia 30334-1300
(404) 656-2647

Attorneys for Respondents

(3)

No. 06-1287

IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION of the State of Georgia; Bart L. Graham, as Commissioner of Revenue of the State of Georgia; Russell W. Hinton, as State Auditor of the State of Georgia; and Gena L. Abraham, as Director of the Georgia State Properties Commission,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

REPLY BRIEF

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Avenue, NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON, BEARMAN, CALDWELL & BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

* Counsel of Record

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WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

RULE 29.6 STATEMENT

The Rule 29.6 statement in the petition is current.

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REPLY BRIEF

The Eleventh Circuit stated succinctly why certiorari should be granted in this case: "This appeal presents a question about state taxation of railroad properties that was expressly left open by the Supreme Court of the United States, has since divided the federal appellate courts, and involves the traditional balance of federal and state power." Pet. App. 1a. Respondents' attempts to contradict the impartial views of the Eleventh Circuit regarding the circuit conflict are unavailing.

Not only is there a clear circuit conflict in need of resolution by this Court, but this is a case of high importance. The 4-R Act, passed against a long history of state discrimination in the taxation of interstate railroads, is an essential safeguard of the financial health of the rail industry. The rule adopted below forces a federal district court charged with determining the "true market value" of railroad property to accept "all nonfactual determinations . . . [by the State's appraiser] in constructing a valuation process, regardless of how broad or narrow they may be." Pet. App. 17a. That rule ignores the clear language of the statute, frustrates the statute's fundamental purpose of preventing discriminatory taxation, and opens a gaping loophole through which States can extract a disproportionate share of tax revenue from interstate railroads without fear of federal remedy. Indeed, Georgia's valuation of the taxable railroad property of CSXT has more than doubled since 2001 (from $378 million to $762 million), and from 2005 to 2006 alone railroad property valuations in Georgia escalated by 46.6% whereas other centrally assessed commercial and industrial property increased only 5.6%. Pet. 7, 20-21. Other States have shown similar aggressiveness in adopting breathtaking increases in valuation of rail property. *Id.* at 21-22. Respondents evade rather than answer these points. This Court's review is imperative.

1. The court below deepened an existing, mature split among the Circuits, expressly declaring that it was siding with the Fourth Circuit in conflict with the Second and Ninth Circuits. Pet. 9-10; Pet. App. 10a. Respondents concede that the court below adopted the rule of the Fourth Circuit. Opp. 8, 10. However, respondents argue that the Eleventh Circuit was wrong to declare its rule to be in conflict with the Second and Ninth Circuits. *Id.* at 13-16. That is patently incorrect.

Respondents make much ado about the fact that *Consolidated Rail Corp.* v. *Town of Hyde Park*, 47 F.3d 473 (2d Cir. 1995), "involved only the grant of a preliminary injunction," and that the test for the preliminary injunction "was met even when using the state's own value for the railroad property." Opp. 10; see also *id.* at 13-14. These points are simply irrelevant. While the Second Circuit did not resolve Conrail's *claim* on the merits because the issue at the preliminary injunction stage was simply "whether . . . the district court had reasonable cause to believe that a violation of the 4-R Act had occurred or was about to occur," 47 F.3d at 480, it did in the course of determining the propriety of the preliminary injunction decide the pure question of statutory interpretation of the 4-R Act. The Second Circuit expressly rejected the Fourth Circuit's decision of *Chesapeake Western Railway* v. *Forst*, 938 F.2d 528 (4th Cir. 1991), thereby creating an acknowledged circuit split: "The *Chesapeake* court viewed the method of appraisal as a matter of state policy that was beyond the reach of the 4-R Act. *We do not accept that interpretation of the statute*." 47 F.3d at 482 (emphasis added).

The precedential force of the Second Circuit's decision on a pure question of law is not affected either by the procedural posture of the case or by the Second Circuit's preliminary observation that on a "simplistic level . . . it *appears* that the district court had reasonable cause" to find a 4-R Act violation even under the State's valuation method. *Id.* at 480 (emphasis added). Courts routinely decide questions of law on preliminary injunction appeals; they do not merely address whether

the district court had "reasonable cause" to construe the law as it did.[1] The Second Circuit in *Consolidated Rail* announced a statutory construction that is binding in its jurisdiction, and that rule is in acknowledged conflict with the rule of both the Fourth and Eleventh Circuits.

Similarly unavailing is respondents' attempt to distinguish the Ninth Circuit's decision in *Burlington Northern Railroad* v. *Department of Revenue*, 23 F.3d 239 (9th Cir. 1994). Opp. 10. The Ninth Circuit did decline to decide whether to follow the Fourth Circuit's decision in *Chesapeake Western* (which involved a broader methodological question than was at issue in *Burlington Northern*). 23 F.3d at 240. However, respondents ignore the Ninth Circuit's actual holding: namely, that it was "proper" that "*the district court did not blindly accept the state's valuation method*," but instead "simply gave substantial deference to it," given that under applicable Washington law "the determination of the value of the property by public officials" "may be defeated only by evidence that is 'clear, cogent and convincing.'" *Id.* at 240-41 (quoting RCW 84.40.0301(1)) (emphasis added); see also *id.* at 241 (holding that the district court had "correctly applied" the Washington law standard); cf. 49 U.S.C. § 11501(c) ("[t]he burden of proof in determining assessed value and true market value is governed by State law").[2] Thus, respondents, not the court

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[1] *See, e.g.*, *This That & The Other Gift & Tobacco, Inc.* v. *Cobb County*, 439 F.3d 1275, 1284-85 (11th Cir. 2006) (holding "this Court's prior legal conclusion was binding on the district court, just as it is now binding on us" even though it was rendered at the preliminary injunction stage); *Nicholas v. Goord*, 430 F.3d 652, 659, 662-63, 664 (2d Cir. 2005) (applying rule of Court in *City of Indianapolis* v. *Edmond*, 531 U.S. 32 (2000), decided on appeal of a preliminary injunction denial), *cert. denied*, 127 S. Ct. 384 (2006); *New York Stock Exch., Inc.* v. *New York, N.Y. Hotel LLC*, 293 F.3d 550, 556-57 (2d Cir. 2002) (applying rule of Second Circuit regarding Lanham Act in *TCPIP Holding Co.* v. *Haar Commc'ns, Inc.*, 244 F.3d 88 (2d Cir. 2001), decided on appeal of a preliminary injunction grant).

[2] Respondents argue that the Ninth Circuit forecloses CSXT's position (which is based on precedent of this Court) that market value is a fact

below, "misapprehend[] the basis of the Ninth Circuit's decision." Opp. 15. Thus, regardless of whether *Burlington Northern* conflicts with *Chesapeake Western*, it indisputably conflicts with the rule below that the district court must accept "all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be," and accordingly should exclude any contrary evidence offered by the railroad on valuation methods. Pet. App. 17a. Not surprisingly, the Eleventh Circuit has declared a conflict with the Ninth Circuit as well as the Second. *Id.* at 10a. Respondents' effort to discredit the Eleventh Circuit's assessment fails.

2. Respondents' defense of the Eleventh Circuit rule on the merits also lacks force. Respondents mistakenly argue that the "clear statement" rule applies to this case because of federalism concerns and because CSXT does not dispute that the clear statement rule applies. Opp. 16-18. As an initial matter, respondents mischaracterize CSXT's position. CSXT argued that the meaning of the statutory term "true market value" is plain and satisfies any clear statement rule, but "[r]egardless, the Eleventh Circuit's invocation of the 'clear statement rule' is improper." See Pet. 16-17.

The clear statement rule applies to disputed interpretations of a federal statute that would "alter the 'usual constitutional balance between the States and the Federal Government.'" *Gregory* v. *Ashcroft*, 501 U.S. 452, 460-61 (1991). Thus, in *Department of Revenue* v. *ACF Industries, Inc.*, 510 U.S. 332

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question to be decided on all appropriate evidence, Opp. 15-16, but they confuse separate issues. The Ninth Circuit held that the district court accords deference to the State's valuation where the railroad has the burden of proving market value by clear and convincing evidence. That is not inconsistent with CSXT's position that—regardless of burden of proof—the district court should make a factual determination of "true market value" based on all relevant evidence, including evidence of the proper methods for ascertaining "true market value." In any event, the burden of proof in Georgia is preponderance of the evidence. Pet. App. 37a.

(1994), this Court applied the clear statement rule in deciding whether a different subsection of the 4-R Act—Subsection 11501(b)(4)—deprived the States of the fundamental sovereign power to grant certain commercial and industrial entities tax exemptions that were not extended to railroads. This Court found no such clear statement in the ambiguous terms of subsection (b)(4), which "did not state whether exemptions are a form of forbidden discrimination against rail carriers, and further did not provide a standard for courts to distinguish valid from invalid exemption schemes." 510 U.S. at 343.

The clear statement rule does not apply every time a federal law touches upon an aspect of state sovereign power. Moreover, it is quite a stretch to claim that having a federal district court perform the commonplace judicial task of finding the fact of a property's true market value would somehow "alter the 'usual constitutional balance between the States and the Federal Government.'" *Gregory*, 501 U.S. at 460-61.[3]

Respondents misconceive the function and effect of Section 11501(b)(1). As the legislative history that respondents recite makes clear, a district court that finds a violation of subsection (b)(1) does not issue an injunction dictating what valua-

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[3] Indeed, it can hardly be claimed that subsection (b)(1)'s prohibition against direct discrimination against interstate railroads would alter the constitutional balance between federal and state governments. "It has long been accepted that the Commerce Clause . . . directly limits the power of the States to discriminate against interstate commerce," and "[t]hus, state statutes that clearly discriminate against interstate commerce are routinely struck down." *New Energy Co. of Ind.* v. *Limbach*, 486 U.S. 269, 271, 273-74, 280 (1988); *Maryland* v. *Louisiana*, 451 U.S. 725, 754, 760 (1981) (recognizing the cardinal principle that the "State's right to tax interstate commerce is limited" and holding the tax "is unconstitutional under the Commerce Clause" and judgment "enjoining further collection of the [t]ax shall be entered"). Furthermore, respondents' federalism arguments are particularly ironic on the facts of this case, where the methodology was not adopted in a state statute or regulation, but only by a single appraiser who, respondents concede, changed the previous state appraiser's chosen methodology. Opp. 4.

tion and assessment methods a State may use in imposing taxes, and States may use whatever methods they like. See S. Rep. No. 90-1483, app. B at 22 (1968); *Common and Contract Carrier State Property Tax Discrimination: Hearing on H.R. 16245 Before the Subcomm. on Transp. and Aeronautics of the H. Comm. on Interstate and Foreign Commerce*, 91st Cong. 132-33, 137-38 (1970) (statement of Philip M. Lanier). Section 11501 performs the very different function of a federal check on discrimination against interstate railroads. The railroads seek only to introduce evidence in order to prove the existence and degree of discrimination. Whatever methods the State employs, the end result is measured against the federal discrimination standard, 49 U.S.C. § 11501(b)(1), and the federal court may only intercede to grant injunctive relief when "the ratio of assessed value to true market value of rail transportation property *exceeds by at least 5 percent* the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction," *id.* § 11501(c) (emphasis added). The 4-R Act is thus quite deferential to States; it prohibits discrimination, but does not otherwise dictate how the State exercises its power to tax property within the State.

Thus, contrary to the claims of respondents, the question of statutory interpretation presented here has nothing to do with depriving States of "'a policy choice.'" Opp. 12 (quoting *Chesapeake Western*, 938 F.2d at 531). "True market value" is simply a factual determination necessary to adjudication of a federal discrimination claim. Respondents' objections that "'federal courts are ill equipped'" to make this determination, and that "[t]he concept of true market value is inherently an approximation," *id.* at 11-12, are unsound. This Court has recognized, even where there is no functioning market that prices the property, the trier of fact may still determine "fair market value" even though such a finding necessarily "involves the use of assumptions." *United States* v. *Miller*, 317 U.S. 369, 374-75 (1943). Congress's use of the phrase "*true*

market value" evinces an intent that federal district courts determine independently the objective market value, and not slavishly follow the State's valuation methodology. See *Burlington N. R.R.* v. *Oklahoma Tax Comm'n*, 481 U.S. 454, 461 (1987) ("It is clear from this language that in order to compare the actual assessment ratios, it is necessary to determine what the 'true market values' are.").

Respondents make the self-serving claim that railroads should be satisfied with contesting factual determinations in the application of the State's methodology, as CSXT was limited to doing below. Opp. 20. But respondents' argument skips over the fact that choice of valuation methods is often the principal means by which state tax authorities accomplish discrimination. The district court candidly acknowledged that it would not consider *any* of the CSXT appraiser's analysis, because it did not use exactly the methodology employed by the State's appraiser. Pet. 8. CSXT can hardly be said to have had the opportunity to prove "true market value" without the opportunity to present its own valuation evidence by a competent appraiser.

In Section 11501(b)(1), "Congress prohibited discriminatory tax rates and assessment ratios *in no uncertain terms*, and set forth *precise standards for judicial scrutiny* of challenged rate and assessment practices." *ACF Indus.*, 510 U.S. at 337, 343 (emphasis added) (internal citation omitted). As the Solicitor General has previously represented to this Court, Pet. 12 n.3, Congress did not establish a federal anti-discrimination rule that state tax authorities could easily evade simply by embedding the discrimination in the choice of methodology. The Eleventh Circuit's rule eviscerates the 4-R Act and creates a stark conflict with the rule of other circuits. This case is a perfect vehicle for this Court to decide the straightforward statutory question presented.

3. There can be no question of the importance of this Court's immediate resolution of this case. CSXT showed in its Petition (at 19-22) that the Eleventh Circuit's rule openly

invites state tax officials to devise discriminatory methods for valuing railroad property. Railroads are handcuffed in proving discrimination even at a time when state appraisers in affected jurisdictions are becoming extraordinarily aggressive in their valuations of the property of railroads running through their States.

Respondents evade the evidence of this real world problem by arguing that the facts regarding "CSXT's 2006 property tax situation—whether in Georgia, Florida, or any other State—is [not] part of the record in this case," and these facts "therefore should just be ignored." Opp. 21. That is a red herring. This Court never relies simply on record evidence in assessing the practical importance of a question presented and the need for this Court's intervention, for the simple reason that those issues are not tried in the district court or relevant to the decision of the court of appeals. Significantly, respondents do not dispute any of CSXT's representations even as to their own 2006 practices (which are clearly within their knowledge). *Id.* at 21-22. Most tellingly, respondents do not even attempt to justify why valuations of railroad taxable property jumped 46.6% in 2006 while valuations of other centrally assessed commercial and industrial taxable property only increased 5.6%. *Id.*; see Pet. 20-21.

Respondents also ask this Court to disregard the increasing divergence in state valuations of CSXT's unit value: Georgia and Florida valued the CSXT system at $11.2 and $12.9 billion respectively in 2006, compared to an average in the other unit value States in the Fourth and Eleventh Circuits of $7.1 billion. Opp. 21-22; see Pet. 21-22. Their only justification is to cite the *Burlington Northern* decision approving a district court's exclusion of evidence of compromise values arrived at in negotiations with other States. Opp. 22. Respondents' argument is irrelevant. First, the $7.1 billion average is not based on any "compromise values" agreed to as a result of settlement of litigation or of a formal administrative appeal, and respondents do not suggest otherwise. Second, CSXT is

not seeking to introduce evidence of other States' valuations at trial. CSXT is simply pointing out that such broad and prejudicial divergence on what in theory should be a single number shows the danger of effectively immunizing the State's valuation methods from judicial review, and the need to give the 4-R Act its intended effect.

Respondents argue that state officials are entitled to a presumption that they have properly discharged their public duties. Opp. 21 (internal quotation marks and citations omitted). It is odd for respondents to invoke a presumption that applies only to shift the burden of proof on trial issues, and that of course can be rebutted by evidence.[4] CSXT is not asking for this Court to find wrongdoing; it is merely arguing for the opportunity to prove that the State discriminated—a burden that CSXT must assume under the statute. 49 U.S.C. § 11501(c).

Respondents are thus left attempting to defend their discriminatory tax practices by arguing that "the largest part of the 47% increase in CSXT's 2002 assessment over 2001 was due to" the State's change from using the R-1 reports to the companies' annual reports to shareholders. Opp. 5; see also *id.* at 23. That is yet another red herring. CSXT's appraiser also used the companies' annual reports to shareholders in arriving at a $6 billion unit value. Pl.'s Ex. 1, Tegarden & Associates, Inc., *Appraisal of the Operating Properties of CSX Transportation Inc.* 37-38 (Jan. 1, 2002); see Tr. Vol. 3, at 395-98. The issue in dispute between the parties is whether the 2002 unit value of CSXT was $6 billion (as CSXT maintains) or $8.2 billion (as respondents maintain); the selection of financial reporting data had nothing to do with that diver-

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[4] *See, e.g., United States* v. *Armstrong*, 517 U.S. 456, 464 (1996) ("[I]n the absence of *clear evidence to the contrary*, courts presume that [government agents] have properly discharged their official duties.") (internal quotation marks omitted) (emphasis added); *United States* v. *Chemical Found.*, 272 U.S. 1, 14-15 (1926) (same). Indeed, in the case cited by respondents, *Bracy* v. *Gramley*, 520 U.S. 899 (1997), this Court found "the presumption [was] soundly rebutted." *Id.* at 909.

gence since both appraisers used exactly the same database. CSXT's complaint is that the Eleventh Circuit denied it the opportunity to prove "true market value" of its rail transportation property. Moreover, even if *arguendo* use of financial reporting data had *some* effect on the valuation increase from 2001 to 2002, it cannot explain the increase to $11.2 billion just four years later. Pet. 20-21.[5]

Thus, this Court should grant certiorari not only to resolve the 2-2 split in the circuits, but because of "the importance of the question presented to the States and affected individuals." *Olmstead* v. *L.C. ex rel. Zimring*, 527 U.S. 581, 596 (1999). Congress intended to remedy discrimination against interstate railroads by allowing proof of the "true market value" of railroad property under Section 11501(b)(1), and a comparison of the ratios of assessed to market value of railroad property vis-à-vis other commercial and industrial property. The question of whether a federal district court making the factual determination of "true market value" must accept the valuation method chosen by the State, no matter how discriminatory, is unquestionably of vital significance for both the States and the railroads. This Court's review is imperative.

CONCLUSION

The petition for a writ of certiorari should be granted.

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[5] Respondents also wrongly claim, Opp. 23, that CSXT management's view of the railroad's financial performance was reflected only in the financial reports, and not in the R-1s as well. *See* Tr. Vol. 6, at 886-92 ("I'm not comfortable saying management doesn't rely on information on how the business is doing in the R1. . . . So I'm not saying that the company doesn't rely on information in this report on how the company is operating.").

Respectfully submitted,

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Ave., NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON,
BEARMAN, CALDWELL
& BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

* Counsel of Record

May 7, 2007

Supreme Court, U.S.
FILED
JUL 30 2007
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No. 06-1287

IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION of the State of Georgia; Bart L. Graham, as Commissioner of Revenue of the State of Georgia; Russell W. Hinton, as State Auditor of the State of Georgia; and Gena L. Abraham, as Director of the Georgia State Properties Commission,

Respondents.

On a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

JOINT APPENDIX

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
MATTHEW J. WARREN
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

Counsel for Petitioner

WARREN R. CALVERT*
SENIOR ASSISTANT ATTORNEY GENERAL
THURBERT E. BAKER
ATTORNEY GENERAL
R. O. LERER
DEPUTY ATTORNEY GENERAL
GEORGIA DEPARTMENT OF LAW
40 Capitol Square, S.W.
Atlanta, Georgia 30334-1300
(404) 656-2647

Counsel for Respondents

* Counsel of Record

[Additional Counsel Listed on Inside Cover]

July 30, 2007

PETITION FOR CERTIORARI FILED MARCH 23, 2007
CERTIORARI GRANTED MAY 29, 2007

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Ave., NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON,
BEARMAN, CALDWELL
& BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

PETER J. CROSSETT
JOHN D. COOK
HISCOCK & BARCLAY, LLP
One Park Place
300 South State Street
Syracuse, NY 13202-2078
(315) 425-2814

Counsel for Respondents

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U.S. DISTRICT COURT
NORTHERN DISTRICT OF GEORGIA (ATLANTA)

CIVIL DOCKET FOR CASE #: 1:02-CV-02634-CAP

CSX TRANSPORTATION,

v.

STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA, et al.,

RELEVANT DOCKET ENTRIES

DATE	NO.	PROCEEDINGS
09/26/2002	01	COMPLAINT filed. Consent form to proceed before U.S. magistrate and pretrial instructions given to attorney. FILING FEE $150.00 RECEIPT # 494840 (aet) (Entered: 09/26/2002)
		* * * *
10/16/2002	17	ANSWER by defendants to complaint [1-1]. Discovery ends 3/15/03. (slc) (Entered: 10/17/2002)
		* * * *
12/17/2004	67	Proposed Pretrial Order by CSX Transportation, Inc., State Board of Equalization, Jerry Jackson, Russell W. Hinton, Ray J. Crawford. (Attachments: # 1 attachments part 1 # 2 attachments part 2 # 3 attachments part 3) (als) (Entered: 12/30/2004)
		* * * *

DATE	NO.	PROCEEDINGS
05/13/2005	105	TRANSCRIPT of Proceedings held on 5/17/2005 before Judge Charles A. Pannell, Jr., Court Reporter: Martha Frutchey. (yrm) Modified on 12/7/2005 to correct file date (fem). (Entered: 06/14/2005)
05/13/2005	106	TRANSCRIPT of Proceedings held on 5/18/2005 before Judge Charles A. Pannell, Jr.. Court Reporter: Martha Frutchey. (yrm) Modified on 12/7/2005 to correct file date (fem). (Entered: 06/14/2005)
05/13/2005	107	TRANSCRIPT of Proceedings held on 5/19/2005 before Judge Charles A. Pannell, Jr.. Court Reporter: Martha Frutchey. (yrm) Modified on 12/7/2005 to correct file date (fem). (Entered: 06/14/2005)
05/13/2005	108	TRANSCRIPT of Proceedings held on 5/20/2005 before Judge Charles A. Pannell, Jr., Court Reporter: Martha Frutchey. (yrm) Modified on 12/7/2005 to correct file date (fem). (Entered: 06/14/2005)
05/13/2005	109	TRANSCRIPT of Proceedings held on 5/23/2005 before Judge Charles A. Pannell, Jr.. Court Reporter: Martha Frutchey. (yrm) Modified on 12/7/2005 to correct file date (fem). (Entered: 06/14/2005)

* * * *

DATE	NO.	PROCEEDINGS
09/29/2005	118	ORDER – The Court concludes that the defendants have not discriminated against CSXT in violation of 49 U.S.C. 11501 (b)(4). The Court also holds that the true market unit value of CSXT for the tax year 2002 was $7,726,293,350. The true market value of CSXT's taxable rail transportation property in Georgia for the tax year 2002 was $509,560,171. The defendants, therefore, have not discriminated against CSXT in violation of 49 U.S.C. 11501(b)(1) because the ratio of assessed value to true market value of CSXT's property does not exceed the jurisdictional threshold set out in the 4-R of 42 %. Thus, CSXT is not entitled to relief under the 4-R Act for the tax year 2002. The clerk is DIRECTED to close this file and issue judgement for the defendants in accordance with this ORDER. Signed by Judge Charles A. Pannell on 9/29/05. (dcs) (Entered: 09/29/2005)
09/29/2005	119	CLERK'S JUDGMENT in favor of Defendant against Plaintiff. (dcs) – Please refer to http://www.ca11uscourts.gov to obtain an appeals jurisdiction checklist (Entered: 09/29/2005)
09/29/2005		Civil Case Terminated. (dcs) (Entered: 09/29/2005)

DATE	NO.	PROCEEDINGS
10/26/2005	120	NOTICE OF APPEAL as to 118 Order, 119 Clerk's Judgment by CSX Transportation, Inc. Filing fee $255, receipt number 543364. Transcript Order Form due on 11/9/2005 (fem) (Entered: 10/28/2005)
		* * * *
02/21/2007	140	Certified copy of JUDGMENT of USCA AFFIRMING the decision of the District Court re: 120 Notice of Appeal filed by CSX Transportation, Inc., Case Appealed to USCA Case Number 06-16000. (fem) (Entered: 02/22/2007)

UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

No. 05-16000-CC

CSX TRANSPORTATION, INC.,
Plaintiff-Appellant,

versus

STATE BOARD OF EQUALIZATION, of the State of Georgia, JERRY JACKSON, as Commissioner of Revenue of the State of Georgia, RUSSELL W. HINTON, as State Auditor of the State of Georgia, RAY J. CRAWFORD, as Director of the Georgia State Properties Commission,
Defendants-Appellees

RELEVANT DOCKET ENTRIES

DATE	NO.	PROCEEDINGS
		* * * *
12/19/2006		Judgment Entered
12/19/2006		OPINIA (Notice of issuance of opinion) issued. Costs taxed against the Appellant. c:Charles A. Pannell, Jr.; c:James W. McBride; c:Milo S. Cogan; c:Peter J. Crossett; c: Stephen D. Goodwin; c:Timothy H. Kratz; c: Warren R. Calvert
12/19/2006		Opinion Issued
		* * * *

DATE	NO.	PROCEEDINGS
02/17/2007		The Petition(s) for Rehearing are DENIED and no Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, the Petition(s) for Rehearing En Banc are DENIED.
02/12/2007		REHG1 (Letter enclosing order) issued. c:Betty Jo Christian; c:James W. McBride; c:Milo S. Cogan; c:Peter J. Crossett; c:Stephen D. Goodwin; c: Timothy H. Kratz; c: Warren R. Calvert
		* * * *
02/20/2007		CASE CLOSED-Mandate Issued
02/20/2007		Mandate Issued
02/20/2007		MDT1 (Letter issuing mandate) issued. To: James N. Hatten; c: Betty Jo Christian; c:James W. McBride; c:Milo S. Cogan; c:Peter J. Crossett; c:Stephen D. Goodwin; C: Timothy H. Kratz; c: Warren R. Calvert
03/26/2007		Notice of Filing Certiorari: (SC #06-1287)
06/04/2007		Certiorari Granted: (SC#06-1287)

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

[Filed SEP. 26, 2002]

CIVIL ACTION FILE NO.: 1 02-CV-2634

CSX TRANSPORTATION, INC.
Plaintiff,

v.

THE STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA; JERRY JACKSON, as Commissioner of Revenue of the State of Georgia; RUSSELL W. HINTON, as State Auditor of the State of Georgia; and RAY J. CRAWFORD, as Director of the Georgia State Properties Commission
Defendants.

VERIFIED COMPLAINT FOR INJUNCTIVE AND DECLARATORY RELIEF

1. This is a civil action under 49 U.S.C. § 11501 seeking injunctive and declaratory relief with respect to property taxes that are imposed by the State of Georgia upon plaintiff railroad. As appears more fully herein, plaintiff contends that such taxes discriminate against plaintiff railroad and violate 49 U.S.C. § 11501.

JURISDICTION

2. Jurisdiction of this Court is based upon the following grounds:

(a) Section 306 of Pub.L.No. 94-210, 90 Stat. 54 (Feb. 5, 1976), now codified as 49 U.S.C. § 11501 (referred to herein as "Section 306"), which confers jurisdiction upon district courts of the United States (notwith-

standing 28 U.S.C. § 1341 and without regard to amount in controversy or citizenship of the parties) to prevent a state, subdivision of a state, or any authority of a state or a subdivision of a state, from imposing any tax which results in discriminatory treatment of a common carrier by railroad;

(b) 28 U.S.C. § 1337: As more fully appears herein, this action arises under an Act of Congress regulating commerce; and

(c) 28 U.S.C. § 1331: As more fully appears herein, this action arises under United States Constitution Article I, § 8, Cl.3 (Commerce Clause) and the Fourteenth Amendment to the United States Constitution and presents a federal question.

VENUE

3. The defendants reside in this district, and the claim arises in this district, and thus proper venue lies in this Court under 28 U.S.C. § 1391(b).

PARTIES

4. Plaintiff, referred to herein as "CSXT," is CSX Transportation, Inc.. CSXT is a Virginia corporation with its principal place of business in Jacksonville, Florida, and is an interstate common carrier by railroad. CSXT is duly qualified to do business in the State of Georgia and owns property subject to ad valorem taxation in the State of Georgia.

5. Defendant State Board of Equalization (hereafter sometimes referred to as "the Board") is an agency of the State of Georgia.

6. Defendant Jerry Jackson is the Commissioner of Revenue of the State of Georgia, a member of the Board, and is named as a defendant in his official capacity.

7. Defendant Russell Hinton is the State Auditor of the State of Georgia, a member of the Board, and is named as a defendant in his official capacity

8. Defendant Ray J. Crawford is the Director of the Georgia State Properties Commission, a member of the Board, and is named as a defendant in his official capacity.

AD VALOREM TAXATION IN GEORGIA

9. Pursuant to O.C.G.A. § 48-5-6, all property subject to taxation in Georgia is to be appraised for assessment purposes by the Georgia Department of Revenue ("DOR") at its fair market value.

10. After all non-exempt property in Georgia is purportedly "appraised" at its fair market value, an assessment ratio of 40% is applied to the appraised value to derive the "assessed value" of all property. *See* O.C.G.A. § 48-5-7. It is the "assessed" value against which the property tax rate is applied and taxes are levied and collected.

11. Pursuant to O.C.G.A. § 48-2-18, the Board annually determines and approves a proposed assessment of railroad property, including that of CSXT.

12. Upon information and belief, CSXT alleges that the Board shall issue its proposed assessment in early October 2002. The issuance of a proposed assessment and the notification of such proposed assessments to the counties is the last act required of state officials in the assessment of railroad operating property.

13. Within 30 days after receipt of the proposed assessment, the county board of tax assessors in each county in which CSXT owns property shall make the final assessment. *See* O.C.G.A. § 48-2-18(d). Upon information and belief, CSXT alleges that, as a routine practice, the various county boards of tax assessors adopt the Board's proposed assessments and levy and collect taxes based on the Board's

proposed assessments. Indeed, for the 2001 tax year no county issued a final assessment for CSXT that differed from the proposed assessments issued by the Board.

SECTION 306

14. Section 306 declares that any state tax which results in discriminatory treatment of a common carrier by railroad subject to the jurisdiction of the Interstate Commerce Act constitutes an unreasonable and unjust discrimination against, and an undue burden upon, interstate commerce. Section 306, a copy of which is attached as Exhibit "A", states:

> "[A]ny action described in this subsection is declared to constitute an unreasonable and unjust discrimination against, and an undue burden on, interstate commerce. It is unlawful for a State, a political subdivision of a State, or a governmental entity or person acting on behalf of such State or subdivision to commit any of the following prohibited acts:
>
> "(a) The assessment (but only to the extent of any portion based on excessive values as hereinafter described), for purposes of a property tax levied by any taxing district, of transportation property at a value which bears a higher ratio to the true market value of such transportation property than the ratio which the assessed value of all other commercial and industrial property in the same assessment jurisdiction bears to the true market value of all such other commercial and industrial property.
>
> (b) The levy or collection of any tax on an assessment which is unlawful under subdivision (a).
>
> (c) The levy or collection of any ad valorem property tax on transportation property at a tax rate higher than the tax rate generally applicable to commercial and industrial property in the same assessment jurisdiction.

(d) The imposition of any other tax which results in discriminatory treatment of a common carrier by railroad subject to this part."

15. Section 306(3)(a) defines "assessment" as "valuation for purposes of a property tax levied by any taxing district."

16. Section 306(3)(d) defines "transportation property" to mean "transportation property, as defined in regulations of the [Interstate Commerce] Commission, which is owned or used by a common carrier by railroad subject to this part or which is owned by the National Railroad Passenger Corporation."

17. Section 306(3)(c) defines "commercial and industrial property" to mean "all property, real or personal, other than transportation property and land used primarily for agricultural purposes or primarily for the purpose of growing timber, which is devoted to a commercial or industrial use and which is subject to a property tax levy."

18. CSXT is a common carrier by railroad and is entitled to the protection of Section 306. All of CSXT's property which is the subject of this action is "transportation property" within the meaning of Section 306.

PLAINTIFF'S SECTION 306 CLAIMS

19. Section 306(1)(a) prohibits the assessment of transportation property at a higher ratio to true market value than the ratio of assessed value to true market value of all other commercial and industrial property.

20. "True Market Value" as utilized in Section 306 means fair market value as that term is traditionally defined, and is synonymous with "fair market value" as used in the Georgia statutes.

21. Upon information and belief, CSXT alleges that, after application of the 40% ratio required by O.C.G.A. § 48-5-7, the ratio of assessed value to true market value of all other

commercial and industrial property in Georgia for the 2002 tax year is no more than 40%.

22. CSXT also alleges that since 1996 the property tax on intangible personal property has been repealed in Georgia and that no other locally assessed commercial and industrial taxpayer (other than certain financial institutions) pay tax on intangible personal property.

23. Upon information and belief, CSXT alleges that the Board intends to issue a proposed assessment for CSXT for the tax year 2002 based on the DOR's determination that the system-wide appraised value of CSXT is no lower than $8.2 billion, while the actual true market value of CSXT's taxable operating property is no more than $6 billion.

24. As a result, after application of the 40% ratio required by O.C.G.A. § 48-5-7, the ratio of the assessed value to true market value of CSXT's taxable railroad operating property will be no less than 54.7% and will exceed the ratio applicable to other commercial and industrial real property by more than 5%, in direct contravention of the prohibitions of Section 306(1)(a).

25. Such an excessive and discriminatory assessment results from erroneous appraisal practices by the DOR and the fact that the valuation determined by the DOR contains substantial value attributable to intangible personal property, while locally assessed taxpayers are not subject to tax on intangible personal property.

26. The assessment, levy, or collection of any property tax on the excessive portion of CSXT's valuation will violate Section 306. Unless the defendants, their agents and those acting in concert with them are enjoined and restrained by this Court from assessing, levying, and collecting the taxes based upon these illegal proposed assessments, the plaintiff will be obligated to pay such illegal taxes wrongfully assessed in violation of Section 306.

27. Plaintiff is entitled to a declaratory judgment, order, and decree of this Court determining the proper ratio of assessed value to true market value that may be legally applied to plaintiff's transportation property for the 2002 tax year and an injunction and temporary restraining order enjoining the defendants, their agents and those acting in concert with them, from assessing, levying, or collecting taxes in excess thereof. Plaintiff should not be required to pay such taxes until the lawful taxes are determined.

WHEREFORE, plaintiff prays that this Court:

(a) Determine and decree the proper ratio of assessed value to true market value applied to plaintiff's transportation property above which the defendants are prohibited from assessing plaintiff's transportation property; that this Court issue all necessary and proper prohibitory and mandatory restraining orders and injunctions to effectuate the findings of this Court; and for such other relief as will effectuate the provisions of Section 306 and grant plaintiff full relief; and

(b) Render a declaratory judgment pursuant to 28 U.S.C. § 2201 declaring that the excessive assessment of the plaintiff's rail transportation property, and the imposition, levy, or collection of any taxes based on that illegal assessment, violate Section 306 and constitute an undue and impermissible burden upon interstate commerce; and

(c) Issue a temporary restraining order, and preliminary and permanent injunction to restrain the defendants, their agents, and those acting in concert and participation with them, from assessing, levying, collecting, or imposing any tax on the plaintiff's property based on an assessment in excess of the ratio of assessed value to true market value of other commercial and industrial property; and

(d) Set a date for hearing the plaintiff's application for a temporary restraining order and a preliminary injunction; and

(e) Grant such other equitable relief to which the plaintiff is entitled.

CERTIFICATION

Counsel certifies that the foregoing complies with the font and point selections approved by the Court.

Respectfully submitted,

/s/ Timothy H. Kratz
TIMOTHY H. KRATZ
Georgia Bar No. 429297
Attorneys for Plaintiff

McGuireWoods LLP
Suite 2100, The Proscenium
1170 Peachtree Street, N.E.
Atlanta, Georgia 30309
Telephone: (404) 443-5730
Fax: (404) 443-5784

James W. McBride, Esq.
BAKER, DONELSON, BEARMAN & CALDWELL
555 Eleventh Street, N.W., 6th Floor
Washington, D.C. 20004
Telephone: (202) 508-3400
Fax: (202) 508-3402

Anne Stolee, Esq.
BAKER, DONELSON, BEARMAN & CALDWELL
555 Eleventh Street, N.W., 6th Floor
Washington, D.C. 20004
Telephone: (202) 508-3400
Fax: (202) 508-3402

VERIFICATION

STATE OF GEORGIA
COUNTY OF FULTON

Kerry G. Carnahan, having first been duly sworn, states that he is the Director—Property Taxes for CSXT Transportation, Inc.; that he has read the foregoing Complaint; that the facts stated therein are true to the best of his knowledge, information and belief.

/s/ Kerry G. Carnahan
KERRY G. CARNAHAN

SWORN AND SUBSCRIBED before me
This 25th day September, 2002.

/s/ Toni A. Clark
Notary Public
My Commission Expires:

May 27, 2003

Section 306 of the
Railroad Revitalization and Regulatory Reform Act of 1976
Pub. L. No. 94-210, 90 Stat. 54 (Feb. 5, 1976)

(1) Notwithstanding the provisions of section 202(b), any action described in this subsection is declared to constitute an unreasonable and unjust discrimination against, and an undue burden on, interstate commerce. It is unlawful for a State, a political subdivision of a State, or a governmental entity or person acting on behalf of such State or subdivision to commit any of the following prohibited acts:

(a) The assessment (but only to the extent of any portion based on excessive values as hereinafter described), for purposes of a property tax levied by any taxing district, of transportation property at a value which bears a higher ratio to the true market value of such transportation property than the ratio which the assessed value of all other commercial and industrial property in the same assessment jurisdiction bears to the true market value of all such other commercial and industrial property.

(b) The levy or collection of any tax on an assessment which is unlawful under subdivision (a).

(c) The levy or collection of any ad valorem property tax on transportation property at a tax rate higher than the tax rate generally applicable to commercial and industrial property in the same assessment jurisdiction.

(d) The imposition of any other tax which results in discriminatory treatment of a common carrier by railroad subject to this part.

(2) Notwithstanding any provision of section 1341 of title 28, United States Code, or of the constitution or laws of any State, the district courts of the United States shall have jurisdiction, without regard to amount in controversy or citizen-

ship of the parties, to grant such mandatory or prohibitive injunctive relief, interim equitable relief, and declaratory judgments as may be necessary to prevent, restrain, or terminate any acts in violation of this section, except that—

(a) such jurisdiction shall not be exclusive of the jurisdiction which any Federal of State court may have in the absence of this subsection;

(b) the provisions of this section shall not become effective until 3 years after the date of enactment of this section;

(c) no relief may be granted under this section unless the ratio of assessed value to true market value, with respect to transportation property, exceeds by at least 5 per centum the ratio of assessed value to true market value, with respect to all other commercial and industrial property in the same assessment jurisdiction;

(d) the burden of proof with respect to the determination of assessed value and true market value shall be that declared by the applicable State law; and

(e) in the event that the ratio of the assessed value of all other commercial and industrial property in the assessment jurisdiction to the true market value of all such other commercial and industrial property cannot be established through the random-sampling method known as a sales assessment ratio study (conducted in accordance with statistical principles applicable to such studies) to the satisfaction of the court hearing the complaint that transportation property has been or is being assessed or taxed in contravention of the provisions of this section, then the court shall hold unlawful an assessment of such transportation property at a value which bears a higher ratio to the true market value of such transportation property than the assessed value of all other property in the assessment jurisdiction in which is included

such taxing district and subject to a property tax levy bears to the true market value of all such other property, and the collection of any ad valorem property tax on such transportation property at a tax rate higher than the tax rate generally applicable to taxable property in the taxing district.

(3) As used in this section, the term—

(a) "assessment" means valuation for purposes of a property tax levied by any taxing district;

(b) "assessment jurisdiction" means a geographical area, such as a State or a county, city, township, or special purpose district within such State which is a unit for purposes of determining the assessed value of property for ad valorem taxation;

(c) "commercial and industrial property" or "all other commercial and industrial property" means all property, real or personal, other than transportation property and land used primarily for agricultural purposes or primarily for the purpose of growing timber, which is devoted to a commercial or industrial use and which is subject to a property tax levy; and

(d) "transportation property" means transportation property, as defined in regulations of the Commission, which is owned or used by a common carrier by railroad subject to this part or which is owned by the National Railroad Passenger Corporation.

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

CIVIL ACTION FILE NO: 1:02-CV-2634CAP

CSX TRANSPORTATION, INC.

Plaintiff,

v.

THE STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA; JERRY JACKSON, as Commissioner of Revenue of the State of Georgia; RUSSELL W. HINTON, as State Auditor of the State of Georgia; and RAY J. CRAWFORD, as Director of the Georgia State Properties Commission

Defendants.

ANSWER OF DEFENDANTS

Come now Defendants State Board of Equalization of the State of Georgia ("the Board"), T. Jerry Jackson, in his official capacity as Commissioner of Revenue of the State of Georgia and Chairman and member of the Board, Russell W. Hinton, in his official capacity as State Auditor of the State of Georgia and member of the Board, and Ray J. Crawford, in his official capacity as Director of the Georgia State Properties Commission and member of the Board, and answer and defend the Verified Complaint For Injunctive And Declaratory Relief ("the Complaint") in the above styled case as follows:

FIRST DEFENSE

The Complaint fails to state a claim upon which relief may be granted against the Defendants.

SECOND DEFENSE

The relief sought in the Complaint is barred by the Eleventh Amendment, sovereign immunity, and/or principles of comity.

THIRD DEFENSE

The Court lacks subject matter jurisdiction.

FOURTH DEFENSE

The Complaint fails to name as defendants one or more indispensable parties.

FIFTH DEFENSE

Defendants respond to the individual paragraphs of the Complaint as follows:

1.

Admit that this is a civil action under 49 U.S.C. § 11501 seeking injunctive and declaratory relief with respect to property taxes that are imposed upon the plaintiff; admit that plaintiff contends that such taxes discriminate against it and violate 49 U.S.C. § 11501; deny the remaining allegations of paragraph 1 of the Complaint.

2.

Admit that plaintiff asserts that jurisdiction exists by virtue of the federal statutes referred to in paragraph 2 of the Complaint; state that such statutes speak for themselves; state that the Complaint is barred by the Eleventh Amendment, sovereign immunity, and/or principles of comity; deny that this Court has subject matter jurisdiction; deny the remaining allegations of paragraph 2 of the Complaint.

3 through 8, inclusive.

Admit the allegations of paragraphs 3 through 8, inclusive, of the Complaint.

9.

States that O.C.G.A. § 48-5-6 speaks for itself; deny that all property subject to ad valorem taxation in Georgia is appraised by the Georgia Department of Revenue; deny the remaining allegations of paragraph 9 of the Complaint.

10.

State that paragraph 10 of the Complaint consists of legal assertions rather than factual allegations and therefore requires no response; state further that O.C.G.A. § 48-5-7 speaks for itself.

11.

Admit that the Board annually examines and approves the digest of proposed assessments of railroad companies' property, including that of the plaintiff, prepared by the Property Tax Division of the Georgia Department of Revenue; admit that the Board's duties and responsibilities in that regard are set forth in O.C.G.A. § 48-2-18; deny the remaining allegations of paragraph 11 of the Complaint.

12.

Deny the allegations of paragraph 12 of the Complaint.

13.

State that O.C.G.A. § 48-2-18(d) speaks for itself; admit that county boards of tax assessors often adopt proposed assessments approved by the Board and levy and collect taxes based on the same valuations; deny the last sentence of paragraph 13 of the Complaint for lack of information or knowledge sufficient to form a belief as to the truth thereof; deny the remaining allegations of paragraph 13 of the Complaint.

14 through 17, inclusive.

State that Section 306 of Pub. L. No. 94-210 speaks for itself.

18.

Deny that the plaintiff is entitled to any relief; admit that plaintiff is a common carrier by railroad; deny the remaining allegations of paragraph 18 of the Complaint for lack of information or knowledge sufficient to form a belief as to the truth thereof.

19.

State that Section 306 of Pub. L. No. 94-210 speaks for itself.

20.

State that paragraph 20 of the Complaint consists of legal assertions rather than factual allegations and therefore requires no response.

21.

Deny the allegations of paragraph 21 of the Complaint for lack of information or knowledge sufficient to form a belief as the truth thereof.

22.

Deny the allegations of paragraph 22 of the Complaint.

23.

State that the Board has not yet been presented with the proposed assessment of plaintiff for the 2002 tax year prepared by the Property Tax Division of the Georgia Department of Revenue; admit that the Property Tax Division has determined that the plaintiff's system-wide fair market value is no lower than $8.2 billion; deny the remaining allegations of paragraph 23 of the Complaint.

23

24 through 27, inclusive.

Deny the allegations of paragraphs 24 through 27, inclusive, of the Complaint.

28.

Deny each and every allegation of the Complaint not hereinbefore specifically admitted, qualified, or denied,

29.

Deny that the plaintiff is entitled to any of the requested relief.

WHEREFORE, having fully answered, the Defendants pray that the Court:

(1) Dismiss the Complaint or enter judgment thereon in favor of Defendants and against the plaintiff; and

(2) Grant such other and further relief as it deems proper and just under the circumstances.

CERTIFICATION

Counsel certifies that the foregoing has been prepared using one of the font and point selections approved in LR 5.1B, NDGa.

This 16th day of October, 2002.

THURBERT E. BAKER 033887
Attorney General

DANIEL M. FORMBY 269350
Deputy Attorney General

/s/ Warren R. Calvert
WARREN R. CALVERT 105341
Senior Assistant Attorney General

PLEASE ADDRESS ALL
CORRESPONDENCE TO:

WARREN R. CALVERT
Senior Assistant Attorney General
132 State Judicial Building
Atlanta, Georgia 30334
Telephone: (404) 656-2647
Facsimile: (404) 657-3239

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

[Filed DEC. 17, 2004]

CIVIL ACTION FILE NO 1:02-CV-2634CAP

[Conference is Requested]

CSX TRANSPORTATION, INC.,
Plaintiff,

VS.

THE STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA; BART L. GRAHAM as Commissioner of Revenue of the State of Georgia; RUSSELL W. HINTON, as State Auditor of the State of Georgia and RAY J. CRAWFORD, as Director of the Georgia State Properties Commission
Defendants.

JOINT PRE-TRIAL ORDER

* * * *

ATTACHMENT E TO PRETRIAL ORDER
STIPULATED FACTS

1. CSX Transportation, Inc. ("CSXT") is an interstate carrier by rail that operates in more than 71 counties in the state of Georgia.

2. CSXT, the taxpayer in this case, is a wholly-owned subsidiary of CSX Corporation.

3. The defendants are the State Board of Equalization and its individual members, including Bart L. Graham as State Commissioner of Revenue.

4. The appraised and assessed values of most property in Georgia is determined by local county boards of assessors. The parties refer to this property as "locally-assessed" property. Pursuant to O.C.G.A. § 48-5-6, most locally-assessed property subject to taxation in Georgia is to be appraised for assessment purposes at its fair market value. After any such non-exempt locally-assessed property in Georgia is "appraised" at its fair market value, an assessment ratio of 40% is applied to the appraised value to derive the "assessed value". *See* O.C.G.A. § 48-5-7. It is the "assessed" value against which the property tax is levied and collected.

5. Companies classified in Georgia as "public utilities" are commonly referred to as "centrally-assessed" taxpayers. Centrally-assessed taxpayers include railroads, investor-owned electric utilities, investor-owned telephone companies, pipeline companies, and gas distribution companies. The State Revenue Commissioner issues proposed assessments of the operating and non-operating property of public utilities.

6. The Property Tax Division of the Georgia Department of Revenue annually prepares a proposed assessment of the Plaintiff's railroad transportation operating properties for each and every Georgia county and municipality in which Plaintiff's taxable property is located.

7. In valuing the Plaintiff's railroad transportation operating property for 2002 ad valorem tax purposes, the Department used the unit rule method. The parties agree that the unit rule method is appropriate under Georgia law.

8. Pursuant to the unit rule method the Department first determined the value of the Plaintiff's railroad as an entire operating system irrespective of where the operating property is located and without functional or geographic division of the whole into its component parts.

9. For purposes of the proposed assessment issued to CSXT for the 2002 tax year, the Department determined that

the fair market value on a system unit basis for CSXT was no less than $8.2 billion as of January 1, 2002.

10. The Department estimated a working capital adjustment of $400 million and deducted that from the unit value estimate to eliminate the effect of certain intangible assets.

11. The Department allocated the adjusted unit value estimate of $7.8 billion to the State of Georgia by using the percentage of Georgia road miles to system road miles. For the tax year 2002 the percentage so applied equaled 7.194059%, resulting in an allocated value of $561,136,602. To arrive at CSXT's Georgia taxable fair market value the Department then deducted amounts for motor vehicles (which are separately valued and assessed for ad valorem tax purposes), exempt pollution control equipment and an exempt railroad line. The amount so determined equaled $514,862,671 and was presented to the State Board of Equalization for its approval in November 2002.

12. Following the Board's approval, the Department issued a notice of proposed assessment dated November 25, 2002 to CSXT, which reflected the following a) the Department's distribution of what had been determined as the total taxable fair market value of CSXT's operating property in Georgia among the various counties and municipalities in which the railroad had taxable property, and b) a proposed assessment for each such local jurisdiction, which was derived by multiplying the county's or municipality's distributed value by an assessment ratio that was either the statutorily mandated 40% or the prevailing level of assessment in that county as shown by a sales ratio study performed by the State Auditor.

Tegarden & Associates, Inc.
105 Point East Drive,
Nashville, TN 37216-1403
Telephone 615-226-2300

APPRAISAL
OF THE
OPERATING PROPERTIES
OF
CSX TRANSPORTATION INC.

AS OF
JANUARY 1, 2002

[PLAINTIFF'S EXHIBIT 1]

29

APPRAISAL
OF THE
OPERATING PROPERTIES
OF
CSX TRANSPORTATION INC.

AS OF

JANUARY 1, 2002

- BY -

TEGARDEN & ASSOCIATES, INC.

105 POINT EAST DRIVE

NASHVILLE, TENNESSEE 37216-1403

(615) 226-2300

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Tegarden & Associates, Inc.
105 Point East Drive,
Nashville, TN 37216-1403
Telephone 615-226-2300

November 14, 2003

Mr. James McBride
Baker, Donelson, BeaRman & Caldwell, PC
Lincoln Square
555 Eleventh Street, N.W. - 6th Floor
Washington, DC 20004

Re: Valuation of the operating properties of CSX Transportation Inc. as of January 1, 2002

Dear Mr. McBride:

In accordance with your request we have completed an appraisal of the operating properties of CSX Transportation Inc. as of January 1, 2002. Included in the operating properties are all real, personal, tangible and intangible property owned or used by CSX Transportation Inc. in its railroad business. The purpose of this appraisal is to estimate the market value of the operating properties of CSX Transportation Inc. which operates the largest railroad system in the eastern United States.

We have inspected and analyzed the financial records, gathered the necessary data, and made certain analyses that have enabled us to form an opinion of market value. The market value of the subject property in fee simple interest as defined in the appraisal report, as of January 1, 2002, was

SIX BILLION DOLLARS

($6,000,000,000)

The narrative appraisal report that follows describes the processes used in reaching conclusions, sets forth the assumptions and limiting conditions, and contains relevant data amassed

during our examination. This letter must remain attached to the report in order for the value opinion set forth to be considered valid. This report was prepared for and our professional fee billed to you. It is intended only for use by you, your internal management, and appropriate taxing authorities. It may not be distributed to or relied upon by other persons or entities without our written permission. If you have questions concerning the report, please contact us at (615) 226-2300.

Sincerely,

/s/ Thomas K. Tegarden
THOMAS K. TEGARDEN, MAI, CAE

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Summary of Salient Facts and Conclusions

1. Subject Property:	The operating properties of CSX Transportation Inc. (real, personal, tangible, and intangible owned and used)
2. Interest Appraised:	Fee simple interest
3. Type of Property:	A railway system operating over approximately 40,520 miles of track as of December 31, 2001
4. Area of Operation:	23 States in the United States and 2 Canadian Provinces
5. Purpose of Appraisal:	To estimate the market value of the operating properties of CSX Transportation Inc.
6. Date of Appraisal:	January 1, 2002
7. System Market Value Opinion:	$6,000,000,000
Cost Approach	$6,150,000,000
Income Approach	$5,983,000,000
Stock and Debt Approach*	$9,637,000,000

* Unadjusted for minority discount and liquidity premium.

Purpose of the Appraisal

The purpose of this appraisal is to estimate the market value of the operating properties of CSX Transportation Inc. (CSXT). The value opinion in this appraisal report is the market value as of January 1, 2002. The intended use of this appraisal is for assistance to the legal and property tax representatives of the Company in exercising their duties. This is a business valuation appraisal report prepared in accordance with Standards Rule 10-2, *Uniform Standards of Professional Appraisal Practice*, 2003 Edition, Appraisal Standards Board of the Appraisal Foundation. The value opinion in this appraisal report is the market value as of January 1, 2002, and is prepared for James McBride, Baker, Donelson, Bearman & Caldwell, PC, Lincoln Square, 555 Eleventh Street, N.W. - 6th Floor, Washington, DC 20004.

Description of Subject Property

The subject property of this report is the fee simple interest in all the operating properties, tangible and intangible, used in the operation of CSX Transportation Inc. Fee simple interest is defined as "*absolute ownership unencumbered by any other interest or estate, subject only to the limitations imposed by the governmental powers of taxation, eminent domain, police power, and escheat.*"[1] The operating properties consist of a broad spectrum of properties of a diverse nature, which include real, personal, tangible, and intangible property operated collectively by CSX Transportation Inc. to provide railway services to its customers. (*Where intangibles are not subject to ad valorem taxation, their value should be deducted from the unit value found in this appraisal. The contribution of all leased property used by CSXT in its railway operations is included in the value found in this report.*)

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[1] *The Appraisal of Real Estate*, 11th ed., (Chicago: Appraisal Institute, 1996), 137.

Definition of Market Value

The definition of market value is:

> The most probable price, as of a specified date, in cash, or in terms equivalent to cash, or in other precisely revealed terms, for which the specified property rights should sell after reasonable exposure in a competitive market under all conditions requisite to fair sale, with the buyer and seller each acting prudently, knowledgeably, and for self-interest, and assuming that neither is under undue duress.[2]

The *Standards of Professional Practice* of the Appraisal Institute require that the following items directly related to a market value definition must be included in every appraisal report.

1. Identification of the specified property rights to be appraised.
2. Statement of the effective date of the value opinion.
3. Specification of whether cash, or terms equivalent to cash, or other precisely described financing terms are being assumed as the basis of the appraisal.
4. If the appraisal is conditioned upon financing or other terms, specification of whether the financing or terms are at, below, or above market interest rates and/or contain unusual conditions or incentives. The terms of above-or below-market interest rates and/or other special incentives must be clearly set forth; their contribution to, or negative influence on, value must be described and estimated; and the market data support-

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[2] Appraisal Institute, *The Appraisal of Real Estate*, 11th ed., (Chicago: Appraisal Institute, 1992), 22.

ing the valuation estimate must be described and explained.[3]

The value opinion found in this appraisal, to comply with the above-stated definition of market value, must be in terms equivalent to cash in U.S. dollars.

Function and Scope of Appraisal

The function of the appraisal is to determine the market value of the operating properties of CSX Transportation Inc., for ad valorem tax purposes according to law. The scope of this appraisal includes a comprehensive examination of all relevant financial data necessary for the determination of the market value of the operating assets of CSX Transportation Inc.

Economic Environment

2000-2001 Economic Recap

In early December 2000, most economists projected a soft landing for the economy during 2001. During the preceding five years, healthy financial markets and rapid increases in technology spending propelled the U.S. economy forward. The Country's growth cycle proved surprisingly sound, even in the face of external shocks such as the 1997 Asian financial crisis and the Russian credit-market panic of 1998. In the aftermath of both crises, output continued to expand, despite fears of a slowdown.[4]

However, as the first quarter of 2001 evolved, America's record-breaking expansion grew vulnerable. Technology demand weakened faster than expected, projections of 2001 sales and profits were revised downward at company after company, including such giants as Microsoft Corp. and SBC Communications Inc. Announcements of big workforce cuts

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[3] *Ibid.*

[4] "Industry Outlook", *Business Week*, January 8, 2001, 88.

became a common occurrence. American companies announced nearly two million job cuts during 2001, more than three times as many layoffs as in 2000.[5]

The slowdown also affected business and consumer spending decisions. Businesses became increasingly reluctant to undertake new investments that would expand productive capacity, and they sharply curtailed travel and other expenditures as sales opportunities diminished and profits declined.

According to the National Bureau of Economic Research, the agency that dates the American business cycle, the U.S. economic expansion that began in March 1991, was the longest peacetime expansion in American history. In September of 2000, the American economy was in its 114th month of expansion. This average was dominated by two long expansions: one ran for 106 months and dominated the decade of the 1960s, and the other ran for 92 months and dominated the decade of the 1980s.

However, the National Bureau of Economic Research placed the start of the economic downturn as March of 2001, thus ending the longest peacetime expansion in U.S. History. The beginning of recessionary times along with the dot.com and tech industry decline, the high oil and gas prices, major corporate layoffs, and the September 11, 2001 assault on the New York twin towers and the Pentagon in Washington, D.C. compounded the economic decline of 2001.

Economic Outlook for 2002

With the United States in a recessionary mode many consumers and economists are pointing their fingers of frustration. Some say Alan Greenspan raised rates too much, others say the rate cuts came too late. Some blame Joel Klein for suing Microsoft and causing the technology sector to chill

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[5] "Nutting, Rex, "Nearly 2 Million Laid Off in 2001," CBS.Market Watch.com, January 3, 2002.

out. Others blame OPEC for raising oil prices. And, not surprisingly, some say it's all Wall Street's fault.

The current recession is unlike any other in the past 30 years. In the past, recessions have been rooted in weak consumer spending, typically induced by high interest rates. Then as consumer demand faltered, businesses would find themselves with unwanted inventories. They would cut back on orders, production and hiring until demand returned. Lay-offs would naturally occur. Eventually, the Federal Reserve would lower interest rates enough to spur demand, restoring growth, once inventories were low again.

However, that's not what happened to the U.S. this time. In fact, sales of homes and autos have remained strong, close to record levels. Consumers, despite the bear market, kept up their spending in 2001. Real consumer spending grew about 5 percent in 1998, 1999, and 2000. It has slowed to about one-half that now, according to Rex Nutting of CBS.Market Watch.com, December 17, 2001. In previous recessions, consumer spending turned negative.

So far, the Federal Reserve's rate cuts have had limited impact. Stock prices are down, longer-term interest rates are only down 10 basis points or so, and the dollar remains strong against other currencies. Despite a massive infusion of money into the economy, financial conditions are largely unchanged from year end 2000.

Economies evolve. Change is gradual and often hard to assess while it is happening. The New Year looks to be a lot better than 2001 because many economic factors are in place today that were missing last year. 2001 was the worst year for the U.S. economy since 1991.

Several important facts are the basis for a positive economic outlook. For one thing, the Federal Reserve cut interest rates 11 times during 2001, bringing the key federal funds rate down below the rate of inflation for the first time since

1994. Additionally, the Federal Reserve has lifted up the money supply also. The money measure known as M2 is, adjusted for inflation, growing at the fastest pace seen in about 30 years, according to Dr. Irwin Kellner, on CBS. MarketWatch.com, December 28, 2001.

On the fiscal side, there's been help as well. A $40 billion tax cut was implemented over the past summer, while spending on defense, national security and other items has gone up, both before and after the September 11, 2001, terrorist attacks. Additionally, energy prices have retreated. Since May of 2001, gasoline prices have fallen by over 50 cents a gallon. So while the economy still appears to be listing, the indicators that tend to look ahead suggest that the U.S. economic recovery is near.[6]

The economy, mired in a recession since March, will struggle to recover before summer of 2002 according to the article, "Economists look for sluggish recovery in 2002," by Rex Nutting in CBS.MarketWatch.com, December 17, 2001. "The recovery will come, but I don't think it'll be a strong recovery," said Irwin Kellner, chief economist at CBS. MarketWatch.com. Kellner is one of the more optimistic economists, figuring the economy will grow 1.5% during 2002. John Ryding, senior economist at Bear Steams reported that the economy during 2002 would be sluggish.

Predictions of growth for 2002 from the economic forecasters follows:

Irwin Kellner, chief economist at CBS.Market Watch.com	1.5%
Blue Chip Economic Forecasts (53 analysts)	1.0%
(In the 3rd & 4th quarter predictions increase to 3.5%)	

[6] Kellner, Dr. Irvin, "It's always darkest before the dawn," cbs.market watch.com, December 28, 2001.

BusinessWeek Forecasters (59 analysts)..... 1.5%
(In the last half of year. . . .3.5%)

Economy.com Inc..... 2.0%

Economists are in agreement that the recession that began in March of 2001 will likely be one of the mildest in the postwar era. By the second half of 2002, forecasters expect real GDP growth to pickup. And by year-end 2002, most economists predict the Federal Reserve to begin lifting interest rates, but only enough to shift monetary policy from its current accommodative mode to a more neutral stance.

The 59 economic forecasters from BusinessWeek warn us not to expect to return to the days of 4% to 5% real growth, soaring profits, and 30% gains in stock prices. They say those days are gone. Instead, look for economic activity that's governed by fundamental relationships. Consumer spending will grow more closely with household income. Capital spending will be guided by profits and cash flow, and stock prices will rise in line with more sensible expectations for risk and reward according to James C. Cooper and Kathleen Madigan in the December 31, 2001 article in BusinessWeek.com.

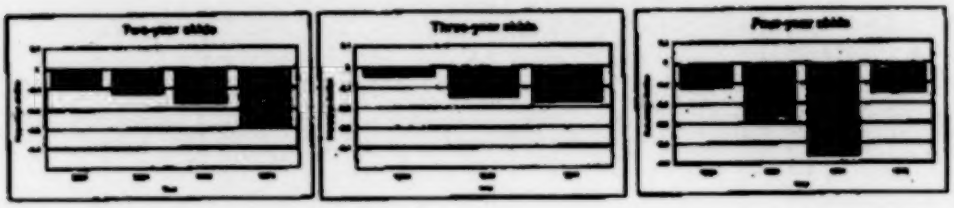
Stock Market

Two years into the 21st century's first bear market and the stock market is partying like it's 1999, according to an article by Mara Der Hovanesian, in BusinessWeek/online, December 31, 2001. The fourth quarter of 2001 rally brought about the highest returns since 1999 led by a 37% surge in the NASDAQ Composite Index since the September 21, 2001 lows. That percentage increase chopped the techladen index' year long losses to two-third those of 2000. The Dow Jones industrial average gained 19% in less than three months, and the Standard & Poor's 500 index climbed 8%. The recent gains in the broader market are impressive, but the Dow is still on tract to lose 8%, and the S&P to lose 13% overall for 2001, according to Hovanesian.

The Dow Jones industrial average will see its first back-to-back losses since the 1977-78 period, when the blue chip barometer declined 17.3% and 3.2%, respectively. And the S&P and NASDAQ will register their first two-year declines since the 1973-74 period.

Investors' pain was widespread in 2001. Using the Wilshire 5000 index as a gauge for the broad market, a total of $1.68 trillion in wealth was wiped out since the start of the year. The broad index is down 12% on the year.

S&P 500 losing streaks chart published in USA Today, January 2, 2002, reported by Bob Laird follows:



Source: Ned Davis Research

One argument that economists make for a sustained stock market rebound is historical precedent. Since World War II there have been ten bear markets which posted average declines of 29% and lasted just 15 months. The current bear market unleashed by the collapse of speculation in Internet stocks, a rout in business capital spending, and a plunge in profits has lasted longer at 19 months. It has also cut deeper, with declines in individual stocks of nearly 40% on average.

The economy and our Nation have been gripped by unusual uncertainties, many due to the terrorist attacks of September 11, 2001. We are in a new world of risk with radically altered markets - and investors will forget the lessons of 2000 and 2001 only at their peril according to an article, "Time to Get Back in the Game - Cautiously," written by Mike McNamee in the December 31, 2001 BusinessWeek/Online.

Thumbing through any current finance magazine will give the reader of this report an idea of how lousy the stock market treated investors during 2001. Investment firms are now pushing bond funds that yield slightly more than 5% according to an article by Adam Shell in January 2, 2002, USA Today, entitled "Single-digit returns might be sign of times." The skimpy 5% bond yield is slightly lower than the high single-digit gains stock investors can expect on average over the next decade, Wall Street experts say. Shell, in his article, reports that some say this is a reality check, a return to sanity, an end of an era. There is a growing consensus on Wall Street that tomorrow's stock returns will be far less exuberant than yesterday's gains.

Many experts believe the stock market is in the process of returning to more normal, or average returns after a decade of unusually large gains. It's called "reversion to the mean." Simply put, what goes up is likely to come down, and what goes down is likely to bounce back, according to Shell's article.

Jeremy Siegel, finance professor at the University of Pennsylvania's Wharton School of Business predicts that ours will be a world of lower returns and that people have outsize expectations. Fred Taylor, chief investment officer at U.S. Trust says, "The equity cult is dead." Why? He reports that a realization that the stock mania of the late 1990s was an aberration, not the dawn of a new era as many Wall Street analysts claimed. The clincher was the second down year in a row for the stock market. Investors now have a renewed sense of risk.

For the first time in many years, consumers, investors, stock analysts, economists and the Federal Government are all in agreement on our economy. At some point during 2002, and no one can agree when, our U.S. economy should make a come-back and eliminate the word "recession" from our vocabulary. All feel with the current recession not mirroring

recessions of the past, that coming out of a mild recession will spur mild growth. There is a wide divergence on what exactly that growth will be. Due to so many unusual uncertainties embedded in our current economy the risk level for corporate America is higher than it has been in the last ten years. Additionally fundamental business risk of industry has gone up.

Bonds

Bonds have beaten stocks for two years running. That may change in 2002. Thanks to the Federal Reserve's eleven rate cuts during 2001, short-term U.S. Treasury yields dipped to their lowest levels in decades. However, during the last six weeks of 2001 bond rates began creeping back up amid expectations that the economy would recover during 2002.

"Over the last two years bond investors earned most of their return from price gains, but 2002 will be about yield plays," says Kevin Cronin, chief investment officer for fixed income at Putnam Investments. William H,. Gross, portfolio manager of PIMCO Total Return, the Nation's largest bond fund with $48.8 billion in assets agrees. "Fears of a bear market in bonds over the next 12 months are exaggerated," Gross said in recent comments.

On October 31, 2001 the U.S. Treasury announced that it would stop issuing 30-year bonds, sparking the biggest bond market rally since the 1987 market crash. While the government had discussed eliminating the 30-year bond in the past, the October 31 announcement both surprised and angered bond investors, according to an article by Sandra Block, "Treasury to stop issuing 30-year bonds," at USAToday.com, October 31, 2001. By the end of the day on October 31, 2001, yields on U.S. Treasury bonds, which move in the opposite direction of prices, fell to 4.89%, down from nearly 5.2% the day before.

Many bond analysts believe the U.S. Treasury's main goal in wiping out the 30-year bond was to give the economy a boost by reducing the cost of long-term borrowing. While the Federal Reserve has reduced short-term rates 11 times this year, long-term rates haven't followed. The Federal Reserve generally has called the shots on rates and the Treasury, with this one action, has caused long-term U.S. Treasury yields to drop over 30 basis points in one day, says Bog Auwaerter, senior fixed income portfolio manager for Vanguard Group.

How are corporations handling their heavy debt loads? Since the recession was officially noted in March of 2001, nonfinancial corporations have issued new bonds by the truckload, driving up their total debt by $137 billion. By contrast, during the 1990-1991 recession, nonfinancial corporate debt rose only $5 billion according to an article, "The Threat of a Huge Debt Load," by Michael J. Mandel in "Economic Trends," at BusinessWeek/online, December 31, 2001.

Optimists argue that this time, companies were able to take on new debt and refinance old debt at low interest rates, making it less worrisome. And, interest paid is less than 4% of nonfinancial corporate output, compared with 6% during the last recession.

Nevertheless, new data from the Federal Reserve raises questions about corporate balance sheets. Nonfinancial corporate debt at a share of new worth now stands at 59%, a record level. Moreover, that's up from 54% a year earlier, the biggest four-quarter jump ever. By comparison, the ratio of debt to net worth at the end of the 1990-1991 recession was only 51% according to Mandel.

The high level of debt compared to net worth reduces the financial cushion of companies and makes them more vulnerable to unexpected shocks. For example, if inflation falls more sharply than expected and companies can't raise

their prices, the debt will be harder to repay. Finding flaws in a corporate financial system ahead of time is never easy. But it would be more reassuring if corporate America was not borrowing quite so much. This fact alone raises the investor's financial risk.

Summary

Where did the projected 2001 U.S. economic soft landing go? 2001 began with aggressive Federal Reserve rate cuts and lots of talk about an economic soft landing. With staggering losses from 2000 under their belts, investors figured, with Greenspan's help the U.S. soft landing was imminent. By mid-2001 all talk about a soft landing vanished. The U.S. recession began in March. The September 11, 2001, terrorist attacks in New York and Washington, D.C. produced devastation of unimaginable proportions and threw the economy even deeper in recession according to Jule Rannazzisi at CBS.MarketWatch.com, December 31, 2001.

As 2001 has ended, the U.S. economic recovery appears to be more an economic forecast rather than fact. The last economic data of 2001 indicates that industrial activity is still falling, retailers are showing lackluster sales, and businesses are laying off workers due to poor profits and dim future prospects. Most economists in general predict that the recession will end in 2002. The time period ranging from the first quarter to the last quarter, with more agreement that the recovery will occur during the last half of 2002. The combination of deep interest-rate cuts by the Federal Reserve and last year's tax-rate reductions should have the intended effect of warding off a precipitous downturn.

In an article by James C. Cooper and Kathleen Madigan in BusinessWeek, January 14, 2002, both authors suggest that growth this year will be driven by time-tested fundamentals, not unsustainable fads. Instead 2002, will see the return of the back-to-basics economy. Forget the wealth effect from stock-

price bubbles. Consumer spending in 2002 will grow more in line with gains in take-home pay. Companies will take a more prudent approach to new technology as more realistic expectations about sales and profits will dictate capital budgets.

As recoveries go, however, this one won't be very impressive. The growth rate, measured from the fourth quarter of 2001 to the fourth quarter of 2002, will be in the range of 1% to 3.5% (see chart above), according to the economic analysts reported in this report. Again, most of the analysts feel the economic recovery will likely be in the last half of 2002.

Corporate financial and business risk has not been as high in the last ten years as it is entering the year 2002. Confronting and controlling those risks was the theme of Business Week's Investment Outlook for 2002.

2002 Economic Outlook - Railroad Industry

From a monetary policy perspective, the Federal Reserve responded early in 2001 to signs of economic weakness by lowering short-term interest rates aggressively (eleven times). Longer-term rates, such as those tied to 30-year mortgages fell as well. Businesses were able to take advantage of the lower interest rates to restructure their balance sheets, paying off high debt using lower-interest loans. The federal government also loosened its fiscal policy stance as evidenced by the summer income tax rebate program aimed at stimulating household spending.

Whether the policy measures enacted in the first eight months of 2001 would have been sufficient to prevent the degree of contraction seen in the overall economic activity is not clear according to the Fourth Quarter 2001, EconSouth produced by the Federal Reserve Bank of Atlanta. What is clear, however, is that the tragic events of September 11, 2001, exacted a substantial toll on the Nation's economy, leading to a decline in overall economic activity.

The United States economy entered 2002 on a slowing trend which affected businesses. They became increasingly reluctant to undertake new investments that would expand productive capacity, and they sharply curtailed travel and other expenditures as sales opportunities diminished and profits declined. Much of the freight carried by railroads is extremely sensitive to the economy and, therefore, has experienced a sharp decline in recent months as the United States' economy slowed. W. R. Pekowitz, Jr., in his December 14, 2001, "Railroad Industry" report for *Value Line* said cost-cutting measures and smoother operating networks should allow for continued improvement in railroad operating ratios. Freight demand is highly correlated to business and economic activity. Because of this, the recession has hampered carload volumes at all of the railroads reported Pekowitz.

The year 2001 was quite different for the transportation environment. Coal volumes, which drove much of the railroad revenue gains through the first seven months of 2001, showed signs of contracting the last several months of 2001. Pekowitz reported that *VL* believed the combination of lower natural gas prices, a relatively mild summer coupled with a warm fall, and problems at the coal mines was the blame for much of the decline. The weather situation, according to Pekowitz, has allowed the utilities that rely on coal energy to replenish stockpiles, thereby reducing demand for additional orders. Thus, if the weather does not return to more normal patterns in January and February 2002, coal volumes could be severely hampered through the winter

In the EIA's "Short-Term Energy Outlook - February 2002, released February 6, 2002, very mild winter weather conditions were projected to continue to dampen heating season energy demand patterns. Heating degree-days in January 2002 were about 14-17 percent below normal (depending on the region) and below year-ago levels. For the entire winter heating season (Quarter 4 2001 - Quarter 1 2002), a return to

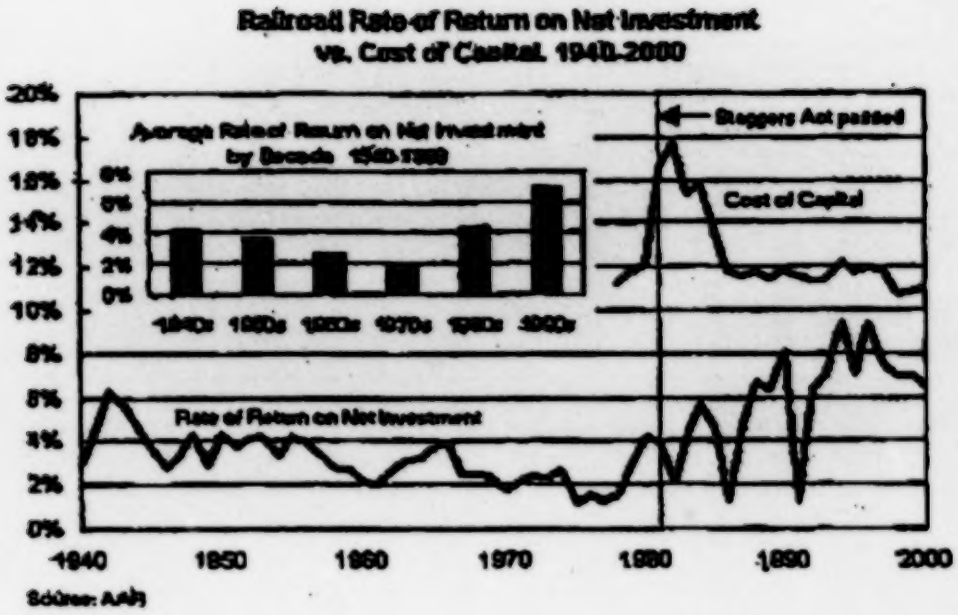
normal for the time remaining will still imply a year-over-year decline of about 17 percent in heating degree days, thus affecting the coal volumes that the rail industry transports. United States based rail carriers, especially Norfolk Southern, CSX, and Burlington Northern Santa Fe, which have relied on coal to support much of their growth of late, will be hard hit and could experience top-line contraction is the EIA's short-term energy outlook is correct, according to *VL's* Pekowitz.

Railroad Industry Performance and Outlook

Railroad Industry — History and Overview

In the 1970s, the cumulative effects of decades of rigid and arcane government regulation brought the U.S. rail industry to the brink of ruin. More than 20 percent of the nation's rail mileage was accounted for by railroads in bankruptcy; return on investment averaged just two percent; and railroads could not afford the massive investments necessary to modernize and maintain their infrastructure. Because the status quo was not tenable, the government had two choices: nationalization, at a continuing cost of billions of dollars, or reliance on the free market. The government wisely chose the free market and passed the Staggers Rail Act of 1980.

In enacting the Staggers Rail Act, Congress recognized that railroads faced intense competition from trucks and other modes for most freight traffic, but prevailing regulation prevented them from earning adequate revenues and competing effectively. Railroad survival required a new regulatory scheme that allowed railroads to establish their own routes, tailor their rates to market conditions, and differentiate rates on the basis of demand. Since then, the rebirth of the railroads has exceeded all expectations.



Mergers and Acquisitions in the Railroad Industry (1995 - 1999)

Railroad profitability has improved since the Staggers Rail Act, but railroads are still not earning competitive returns. Since 1978, the Interstate Commerce Commission (ICC)/ Surface Transportation Board (STB) has annually determined the revenue adequacy of individual Class I railroads. A railroad generates adequate revenue — *i.e.*, it is earning enough to cover all costs of efficient operation, including a competitive return on capital — when its rate of return on net investment (ROI) equals or exceeds the rail industry's current cost of capital (COC). The STB standard is similar to that used by public utility regulators throughout the country. The average rate of return on net investment — which had been falling for decades — rose from an annual average of 2.0 percent in the 1970s to 4.4 percent in the 1980s and 7.0 percent from 1990-2000. The rail industry still falls well short of earning its cost of capital, but the gap has narrowed according to the Association of American Railroads. The graph above, from the *www.aar.org* site, illustrates the point well.

The U.S. freight railroad industry has undergone substantial changes over its 170-year history. Today's freight railroad industry is vital and competitive, due in large part to the reforms enacted in the Staggers Rail Act of 1980.

At the time the Staggers Rail Act was enacted there were about 40 rail carriers that carried freight in the railroad industry. The restructuring of the major railroads ensued as a result of the Staggers Rail Act and partial deregulation. Class I Railroads are U.S. line haul freight railroads with operating revenue in excess of $261.9 million.

Six of the mergers and acquisitions that have occurred from 1995 to 1999 are: (1) Canadian National acquired Illinois Central in 1999; (2) Norfolk Southern acquired a 58% interest in Conrail in 1998; (3) CSX acquired 42% of Contrail in 1998; (4) Union Pacific acquired Southern Pacific in 1996); (5) Union Pacific acquired Chicago/North Western in 1995; and (6) Burlington Northern acquired Santa Fe Pacific in 1995.

Two Canadian railroads, Canadian National Railway and Canadian Pacific Railway, have enough revenue that they would be Class I railroads if they were U.S. companies. Both companies also own railroads in the United States that, by themselves, qualify to be Class I railroads. Two Mexican railroads, Ferrocarril Mexicano and TFM, would also be Class I railroads if they were U.S. companies. The Class I railroads in 2000 were: The Burlington Northern Santa Fe Railway, CSX Transportation, Grand Trunk Western Railroad, Illinois Central Railroad, Kansas City Southern Railway, Norfolk Southern Combined Railroad Subsidiaries, Soo Line Rail-road, and Union Pacific Railroad, according to a February 4, 2002 report on "Class I Railroad Statistics" published by the Association of American Railroads - Policy & Economics Department and provided at their *www.aar.org* website.

Median Return on Equity
Class 1 Railroads vs. Fortune 500 Companies

	Median ROE		No. of	Class 1
Year	Class 1 RRs	Fortune 500 Cos.	Fortune 500 Ind.	RR Rank
1985	5.3%	11.6 %	26	25th
1986	0.0	11.6	25	25th
1987	7.0	13.2	25	24th
1988	8.6	16.2	25	23th
1989	4.3	15.0	25	25th
1990	8.3	13.0	25	23rd
1991	1.0	10.2	25	23rd
1992	7.6	9.0	25	14th
1993	8.0	11.9	35	26th
1994	11.3	13.7	35	27th
1995	5.9	14.0	36	35th
1996	11.6	14.1	38	30th
1997	10.4	13.9	37	30th
1998	11.5	13.4	38	28th
1999	8.8	15.2	41	34th
2000	9.4	14.6	48	40th

Source: AAR, *Analysis of Class I Railroads, Fortune*

Railroad Profitability

For years prior to railroad deregulation in 1980, the term "railroad profits" was an oxymoron. Since enactment of the Staggers Rail Act, rail profitability has improved. Even with their improvements, though, railroad earnings are still not sufficient to cover all costs of rail operations, and railroads generally lag other U.S. businesses with which they compete for capital.

Return on equity (ROE) is a commonly used indicator of short-term profitability. According to Fortune 500 data, in the 16 years from 1985 to 2000, overall railroad ROE was less than the Fortune 500 average each year, and usually lower than the ROE of individual industries which rely heavily upon rail transportation.

In all but 3 of the 16 years, the railroad ROE was in the lowest quartile among Fortune 500 industries. In 8 of the 15 years, at least 92 percent of other industries had higher ROE than the railroads. Similar analyses using data from the S&P 500, *Business Week*, and *Value Line* all yield similar results: Class I railroads typically register returns substantially inferior to those of other industries. The graph on the preceding page depicts the median return on equity of Class I Railroads vs. Fortune 500 Companies and was taken from the *www.aar.org* website.

Likewise, in most of the past 15 years, the dividend yield for the railroad industry has been lower than the S&P 500 average.

The cost of funds from the capital markets depends, in part, on the financial rating of the railroad companies. In general, railroads' ratings are middling to lackluster and at the bottom of so-called "investment grade" bonds. The bond ratings of virtually every major railroad have been downgraded at least once in recent years. Moreover, relatively low profitability is

a major reason why railroad stocks have significantly underperformed the market in recent years.

Price Earnings Ratios and Dividend Yields of Class I Railroads vs. S&P 500 Industries

	P/E Ratio		Dividend Yields	
	RRs	S&P 500	RRs	S&P 500
1985	9.1	12.9	3.5%	4.3%
1986	13.4	15.8	3.4%	3.7%
1987	12.1	16.0	3.0%	3.3%
1988	11.0	11.1	4.5%	3.7%
1989	11.7	13.9	3.5%	3.5%
1990	12.0	15.3	3.6%	3.8%
1991	21.5	22.4	3.5%	3.4%
1992	16.2	21.9	2.3%	3.0%
1993	16.6	20.6	2.3%	2.8%
1994	14.1	15.1	2.4%	2.9%
1995	14.8	15.9	2.2%	2.6%
1996	14.7	17.2	2.0%	2.3%
1997	16.8	27.5	1.9%	1.5%
1998	21.0	32.8	1.9%	1.3%
1999	16.5	32.1	2.0%	1.2%
2000	15.4	27.1	2.9%	1.0%

Source: AAR, various industry reports

In general, railroads fall below those companies which are judged to possess "high quality" or "favorable investment attributes" and above those companies which "face major ongoing uncertainties" and which "lack characteristics of

desirable investment." According to Fortune 500 data, Class I railroads had lower return on assets than the Fortune 500 median in 12 of the 16 years from 1985 to 2000. Compared to industries that are significant rail shippers, railroads had lower return on assets more than two-thirds of the time. Price/earnings ratios and dividend yields are, at best, short-term measures of financial health. Yet even for these, for each of the 16 years from 1985 to 2000, the price/earnings ratio for railroads has been lower than the average ratio for the S&P 500 companies. Likewise, in most of the past 15 years, the dividend yield for the railroad industry has been lower than the S&P 500 average, as the American Association of Railroads graph above indicates. All of the political and economic factors discussed in this section will affect the typical investor's cost of capital as the elements of business and financial risk increase.

Factors Affecting The Railroad Industry

The recent collapse of the Houston-based energy giant Enron Corp. has virtually all the ingredients for scandal in Washington and then some, according to an article January 24, 2002 titled "Enron and Anderson," in opensecrets.org. Enron's imminent collapse quickly landed it in the penalty box. In an age when giant earnings write-offs have become commonplace, it's hard to shock Wall Street. But on November 8, 2001, Enron Corp. managed to do it. After years of high-octane growth, the Houston-based energy company acknowledged that results for the past three years were actually overstated by more than half-billion dollars. This was confirmation of an investor's worst fears, according to an article in BusinessWeek, by Byrnes and Henry, November 26, 2001. Although up to 800 companies have some exposure to the Houston-based energy-trading firm, losses are unlikely to trigger a chain of failures. (Last year was a record one for bankruptcies: 255 stock-market companies filed for Chapter

11 compared with 176 in 2000, a 45 percent increase, according to CBS MarketWatch.com, January 17, 2002.)

According to the National Bureau o f Economic Research, the agency that dates the American business cycle, the U.S. economic expansion that began in March 1991, the longest peacetime expansion in American history, started its economic downturn by March of 2001, thus ending the longest peacetime expansion in U.S. History. The beginning of recessionary times along with the dot.com and tech industry decline, the high energy prices, major corporate layoffs, and the September 11, 2001 assault on the New York twin towers and the Pentagon in Washington, D.C., and the Enron bankruptcy filing compounded the economic decline of 2001. Economists project the turnaround to begin somewhere between the second and last quarter of 2002 with most forecasting the economic rebound to occur the last half of the year.

The overriding theme of the railroad industry appears to be that freight demand is highly correlated to business and economic activity. Because of the United States economic recession, coupled with the economic aftermath of September 11, 2001, carload volumes have been hampered at all of the railroads. The intermodal and metals businesses have been especially hard hit, as these two groups are more reliant on economic activity than other commodities according to W. R. Pekowitz, Jr. in the December 14, 2001, "Railroad Industry," report by *Value Line*. He continued to say that a number of companies have cited the weakening economy as the reason for a less-optimistic earnings. All of the factors listed above point to continued elevated business and financial risk which is reflected in the weighted average flotation adjusted cost of capital.

Brief History and Company Statistics

CSX Transportation Inc. (CSXT or the Company) is an operating Class 1 railroad with operations in the United States and Canada and is engaged principally in the business of railroad transportation. CSXT is a wholly-owned subsidiary of CSX Corporation (CSX), a publicly-owned Virginia corporation with headquarters in Richmond, Virginia. Headquartered in Jacksonville, Florida, CSXT conducts railroad operations in its own name and through railroad subsidiaries.

CSX Transportation Inc. is the largest railroad in the eastern United States. Its rolling stock includes more than 3,600 locomotives and 100,000 railcars, which in 2001 hauled nearly 5.1 million carloads of freight. Headquartered in Jacksonville, Florida, CSXT accounted for 75% of CSX's operating revenue and 78% of operating income in 2001.

Rail shipments include merchandise traffic, automobiles and related products, and coal, coke and iron ore. Merchandise traffic accounted for 57% of rail revenue in 2001, while automotive traffic accounted for 13% and coal, coke and iron ore accounted for 29%. Merchandise traffic includes chemicals, paper and forest products, agricultural products, minerals, metals, phosphates and fertilizer, and food and consumer products. Coal shipments originate principally from mining locations in the eastern United States and primarily supply domestic utility and export markets.

The Company operates various facilities and equipment to support its transportation system, including its infrastructure and locomotives and freight cars. The Company also owns or leases other equipment to support rail operations, including highway trailers, containers and vehicles. Support facilities for rail operations include yards and terminals throughout its rail network, system locomotive shops to perform locomotive servicing and maintenance, a centralized network operations

center for train dispatching and network operations monitoring and management.

Regulation

Rail operations are subject to the regulatory jurisdiction of the Surface Transportation Board (STB) of the United States Department of Transportation (DOT), the Federal Railroad Administration of DOT, the Occupational Safety and Health Administration (OSHA), and state regulatory agencies. The STB, which is the successor to the Interstate Commerce Commission (ICC), has jurisdiction over disputes and complaints involving certain rates, routes, and services, the sale or abandonment of rail lines, applications for line extensions and construction, and consolidation or merger with, or acquisition of control of, rail common carriers. The outcome of STB proceedings can affect the costs and profitability of CSXT's railway business.

Regulations are enforced by the STB and require periodic formal studies of ultimate service lives for all railroad assets. Resulting service life estimates are subject to review and approval by the STB. For retirements or disposals of depreciable rail assets that occur in the ordinary course of business, the asset cost (net salvage value or sales proceeds) is charged to accumulated depreciation and no gain or loss is recognized. For retirements or disposals of depreciable non-operating property, and for all dispositions of land, gains or losses are recognized at the time of disposal. Expenditures that significantly increase asset values or extend useful lives are capitalized. Repair and maintenance expenditures are charged to operating expense when the work is performed.

Mergers and Acquisitions

CSX and Norfolk Southern Corporation (Norfolk Southern) completed the joint acquisition of Conrail Inc. (Conrail) in May 1997. Conrail owns the primary freight railroad system serving the northeastern United States, and its rail

network extends into several midwestern states and into Canada. CSX and Norfolk Southern, through a jointly owned acquisition entity, hold economic interests in Conrail of 42% and 58%, respectively, and voting interests of 50% each. CSX and Norfolk Southern received regulatory approval from the STB to exercise joint control over Conrail in August 1998, and their respective rail subsidiaries subsequently began integrated operations over allocated portions of the Conrail lines in June 1999.

Under this operating plan, CSXT added approximately 4,400 route miles of track in the northeastern and midwestern United States and in Canada to its existing lines concentrated in the Middle Atlantic and southeastern United States. To service the new operations, approximately 5,600 former Conrail employees joined the Company. CSXT now operates a network of approximately 23,000 route miles in 23 states, the District of Columbia, and two Canadian provinces. CSXT employs approximately 35,000 employees across the combined system.

Competition

The business environment in which the Company operates remains highly competitive. Depending on the specific market, deregulated motor carriers, other railroads and river barges may exert pressure on price and service levels. The presence of advanced, high service truck lines with expedited delivery, subsidized infrastructure and minimal empty mileage continues to affect the market for non-bulk, time sensitive freight. The potential expansion of longer combination vehicles could further encroach upon markets traditionally served by railroads.

As railroads streamline, rationalize and otherwise enhance their franchises, competition among rail carriers intensified. Competition is from several Class 1 railroads and numerous

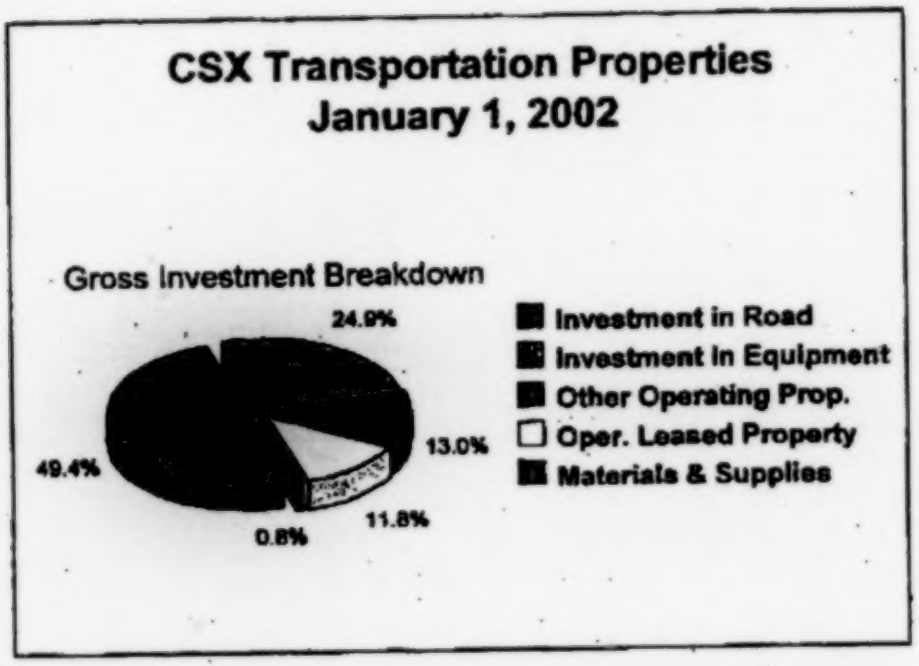
regional railroads and motor carriers that operate in parts of the same territories served by the Company.

Market Risk

The Company is subject to risk relating to changes in the price of diesel fuel. Forward purchase agreements have been entered into with various suppliers for approximately 294 million gallons of fuel, which is approximately 50% of the 2002 requirement, at a weighted average price of 78 cents per gallon. The Company is subject to fluctuations in prices for the remainder of its 2002 needs. A one cent change in the price per gallon of fuel would impact fuel expense by approximately $3 million.

Below is a graph showing a breakdown of CSXT's net investment figures as of December 31, 2001. An organization chart of CSX Corporation, its subsidiaries and affiliates as of December 28, 2001, can be found in the Addendum of this report.

Breakdown of Net investment (Graph)



Appraisal Procedures for Railroad Operating Property

The purpose of this appraisal is to estimate the market value of the operating property of CSX Transportation Inc. The operating physical real and personal property assets of the Company are integral parts of an ongoing business. In this appraisal, we are appraising the *going-concern value* of these integrated assets. The Appraisal Institute defines *going-concern value* as the market value of the tangible and intangible assets of an established and operating business with an indefinite life, as if sold in aggregate.[7] Further, the Appraisal Institute notes that the term *going-concern* has been replaced with *total assets of the business* (TAB), which includes real property, tangible personal property, and intangible personal property.[8]

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[7] Appraisal Institute, *The Appraisal of Real Estate*, 12th ed., (Chicago: Appraisal Institute, 2001), 27.

[8] *Ibid.*, 642.

When appraising all of the operating properties of a railroad company the unit appraisal concept may be applied.[9] Under the unit appraisal concept, the value of the properties being appraised is then determined by measuring their contribution to the overall unit value. The contribution is typically measured by some allocation process. This is a fundamental premise based on the appraisal principle of contribution. The Appraisal Institute defines and discussed the principle of contribution as follows:

> *The concept of contribution states that the value of a particular component is measured in terms of its contribution to the value of the whole property, or as the amount that its absence would detract from the value of the whole.* The cost of an item does not necessarily equal its value. A swimming pool that costs $10,000 to install does not necessarily cause the value of a residential property to increase by $10,000. Rather, the pool's dollar contribution to value is measured in terms of how valuable its benefit or utility is in the market. Its contribution to value might be lower or higher than its cost. Thus, in some cases, a property's market value may not increase even though the physical real estate has undergone alteration, modification, or rehabilitation.[10]

The steps that must be taken in the unit appraisal process are:

1. Determine the unit to be appraised.
2. Estimate the unit or system value.

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[9] The unit appraisal concept is the appraisal of an integrated property as a whole, without reference to the value of its component parts. The unit appraisal concept is the opposite of the *summation appraisal concept*, which is the summing of two or more of the appraisals made of fractional parts of the whole.

[10] Appraisal Institute, *The Appraisal of Real Estate*, 10th ed., (Chicago: Appraisal Institute, 1992), 41.

3. Allocate the appropriate portion of the unit or system to the taxing district.

First, the unit to be appraised is generally the operating property of the railroad company, whether such property is owned or leased. The non-operating properties a railroad company may have are generally appraised individually, independently of the operating unit, or are allocated out of the operating unit.

Second, following the determination of the unit to be appraised, the three indicators or approaches to value are used to determine the market value of the operating property of the railroad company. They are the cost approach, the income approach, and the sales comparison approach. While it may not be possible or practical to use all three approaches in the appraisal process, all should be considered.

Third, once the unit or system value is determined, a proper value is allocated to the taxing district. The allocation process is accomplished through the use of allocation factors which relate to the property being appraised.

There are problems peculiar to the appraisal of integrated business operating properties and these properties are typically best suited to the unit appraisal concept of valuation. Usually a company's property that extends over several taxing districts, such as the property of CSX Transportation Inc., has value and maintains value because it is operated as a system or unit. A railroad company is operated as a unit, provides services as a unit, and reports its financial operating results as a unit. Further, to whatever degree the properties are regulated, the state and federal regulatory authorities essentially exert their regulatory controls and decisions over the operating property as a unit. Thus, the very nature of a railroad company and its property makes it a suitable candidate for the unit appraisal process.

In circumstances where one is dealing with properties that are frequently bought and sold, one would normally have sales of comparable properties to help in the determination of market value. However, in the case of properties the size of the operating property of CSX Transportation Inc., there are not reliable, arms-length comparable sales to help determine the market value. Thus, the appraiser must gather the pertinent operating, financial, and economic information available, determine how it would affect a potential buyer and the seller of the operating properties, and make a judgment determination of the market value of the property.

The three approaches to value — the cost, income, and sales comparison approaches — and how these approaches are applied in the determination of a railroad company's operating property value will be discussed in this report. These three approaches are applicable to all other types of property that are locally appraised or assessed. The same appraisal principles which apply to any type of property, individually appraised/assessed or unit appraised/assessed, are equally applicable to the appraisal of the operating property of a railroad company. The most meaningful appraisal principles in the appraisal of railroad properties are:

1. The *Principle of Anticipation* holds that value is created by the anticipation of future benefits. When appraising income-producing property, such as a railroad, the future benefits are the anticipated future income of the property.

2. The *Principle of Consistent* Use holds that the property must be valued with a single use for the entire property. It is improper to value a property on the basis of one use for a portion of the property and another use for the remainder of the property.

3. The *Principle of Contribution* holds that the value of a component part of a property depends upon how

much it contributes to the value of the whole. This principle is applied in the unit appraisal process as well as in allocating a part of the whole system value to a state or taxing district or to the various component parts of the property.

4. The *Principle of Substitution* holds that a prudent purchaser will pay no more for a property than the cost of acquiring an equally desirable substitute property, having the same level of risk as the subject property, on the open market.

5. The *Concept of Highest and Best Use* is defined as that use among reasonable probable and legal alternative uses which is found to be physically possible, appropriately supported, financially feasible, and which will support the highest present value. When appraising railroad equipment which is a necessary part of the system, the only use permitted by certain governmental restrictions (STB and DOT) and international agreements is the present use; thus making it the highest and best use of the subject property.

Highest and Best Use

The subject of this report includes all the tangible and intangible operating properties owned and used by CSX Transportation Inc. These properties are of a diverse nature and are specifically adapted for use in the railroad industry. While some of the properties could be used in other applications (desks, chairs, certain land and buildings, etc.), the vast majority are specifically designed for railway service.

The properties must be valued at their highest and best use, which means the use that results in the greatest value and is "*. . . legally permissible, physically possible, financially feasible, and maximally productive.*"[11] These tests are often

[11] *The Appraisal of Real Estate*, 11th ed., (Chicago: Appraisal Institute, 1996), 303.

considered in sequence and the tests of legal permissibility and physical possibility must be applied before the remaining test of financial feasibility and maximal productivity. CSXT has been in business as a provider of railway service since 1944. Thus, the current use of the properties is legally permissible and physically possible. The financial feasibility of the use of these properties in railway service has been demonstrated historically leaving only the test of maximal productivity. The railroad industry is currently undergoing changes in many areas. The historical regulations that have limited the operations of railroad companies have been for the most part deregulated. Now however, competitive pressures restrict the use of the property in many ways. Because of the changes in the industry, the risk associated with the operation and ownership of these types of properties is greater now than at any time in the past. Based on the tests applied, it is our opinion that the highest and best use of the subject property in this report is to continue providing railway service.

Next, each of the three approaches and their applicability for appraising the operating property of CSX Transportation Inc. are analyzed and discussed.

The Cost Approach

The cost approach has been considered in the valuation of the operating properties of CSX Transportation Inc. It is important to recognize that sacrificing or expending factors of production does not necessarily establish value equal to the cost or sacrifice. To establish value, the expended factor of production must produce goods or services that have utility — are scarce and in demand in an economic sense. The degree of utility of a good or service is measured, of course, by either the price obtainable or the income that these goods or services can generate. As referenced earlier from *The Appraisal of Real Estate*, ". . . cost does not necessarily equal value." The Institute goes on to state that a property may have much cost and yet have little value.

> Cost is either a retrospective fact or a current estimate. It may or may not have a direct relationship to the utility (present or future) of the property created. Consider, for instance, the classic example of the luxury hotel built in an unpopular location. The hotel might cost much to build but have little value because of the lack of business.[12]

Additionally, the Appraisal Institute notes (as mentioned on page 18) that in discussing business enterprise value the term *going concern* has been replaced with *total assets of the business* (TAB). The Institute goes on to state,

> In assignments involving the market value of the total assets of the business, the cost approach offers little insight.[13]

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[12] American Institute of Real Estate Appraisers, *The Appraisal of Real Estate*, 8th ed., (Chicago: American Institute of Real Estate Appraisers, 1983), 35.

[13] Appraisal Institute, *The Appraisal of Real Estate*, 12th ed., (Chicago: Appraisal Institute, 2001), 643.

Thus, in the appraisal of the TAB of the CSX Transportation Inc. the cost approach can be expected to offer little insight in the estimation of market value.

When considering the cost of railroad property, several types of cost may be analyzed and considered. Some of the cost data that have been considered are:

1. *Original Cost* - The cost at the time a property was originally acquired or constructed and placed into public service.

3. *Reproduction Cost* - The cost of reproducing a new replica property on the basis of current prices, with the same or closely similar material.

4. *Replacement Cost* - The cost of replacing a property with an equally desirable substitute property.

Appraisers cannot categorically accept any of the above costs as market value. There are times when each of these costs would be the same as market value. When a property is new and a proper improvement, the original cost, reproduction cost, and replacement cost could all closely approximate market value. Market value is also affected when a company is unable to earn a return on certain items. In considering the different types of cost, the appraiser must keep in mind the type of property being appraised and consider all government regulations or restrictions placed on the property, or advantages enjoyed by the property.

Each of these costs is intended to be a measure of the value of the subject property when in a new condition. Where the passage of time and use has aged the property, the cost when new must be reduced. This reduction will reflect accrued depreciation from all causes. The three types of depreciation are defined as follows:

1. *Physical Deterioration* - This is the physical wearing out of the property. Deterioration is evidenced by

such physical effects as wear and tear, decay, dry rot, cracks, encrustations or structural defects. It is considered to be the loss in value due to the normal aging process. The level of maintenance of the property affects physical deterioration.

2. *Functional Obsolescence* - This is a loss in value due to certain functional deficiencies or inadequacies within the property itself. In railroad property, functional obsolescence would result from the development of new equipment and machinery that would cause the old equipment to be obsolete before it was physically worn out.

3. *External Obsolescence* - This is the loss in value from causes outside the property itself. Economic forces such as supply and demand and governmental regulations, which place limitations on the company's earning power, result in a loss of value to the property of a railroad company. This loss is external to the property of a railroad company and is measurable as external obsolescence to the railroad company.

The cost approach is used in some form by most appraisers of properties. It is recognized that in valuing a railroad company's property, cost — less an allowance for accrued depreciation — is an item which should be considered in arriving at the market value. Cost can be important even if the property is earning what appears to be an inadequate return.

In the appraisal of the operating property of CSX Transportation Inc., we have attempted to measure all forms of depreciation. We have used the original cost information less physical and functional depreciation, as reported in the Annual Report of CSX Transportation Inc. to the Surface Transportation Board (ACCA-R1) for year ended December 31, 2001. External obsolescence was measured in exactly the same manner stated and directed by recognized appraisal

authorities. *(Please see Explanation of Cost Approach on page 26.)*

In the appraisal of the operating property of CSX Transportation Inc., all types of cost have been given consideration. Original cost less the accrued depreciation (physical, functional, and external) can be used as an indicator of market value by the cost approach provided all forms of depreciation are measured and accounted for.

Either original cost or replacement cost can be used as the basis of the cost approach for the subject property as long as the measurement of depreciation is correctly tailored for each type of cost. If replacement costs were used, more external obsolescence would have to be deducted due to the magnified earnings deficiency based on this type of cost. The use of depreciated replacement cost (after the deduction of all the extra external obsolescence) would produce a figure consistent with the original cost less all depreciation (including a proper adjustment for obsolescence).

On the following page are the computations for the cost approach for the operating property of CSX Transportation Inc.

CSX TRANSPORTATION, INC.
Indication of Value by Cost Approach
January 1, 2002

Investment in Road Property (Sch 330)		$10,887,608,000
Investment in Equipment (Sch 330)		5,477,006,000
Unallocated Items		134,859,000
Other Investment in Railroad Property (Sch 352B)		2,735,196,000
Total Road & Equipment Property		$19,234,669,000
Less: Depreciation and Amortization		4,419,645,000
Depreciation and Amortization (Sch 352A)		707,615,000
Net Road & Equipment Property		$14,107,409,000
Add: Materials & Supplies		181,385,000
Total Net Property + Materials & Supplies		$14,288,794,000
Add Operating Leased Property (Net)		1,702,041,227
Total all Property (owned and leased)		15,990,835,227
Less: Obsolescence adjustment (see below)		
$15,990,835,227 x	61.54%	9,840,759,999
INDICATED VALUE BY COST APPROACH		$6,150,075,228
(Rounded)		$6,150,000,000

Obsolescence / Enhancement Estimate – January 1, 2002

RETURN ON TOTAL NET PLANT (1996-2001)

Year End	Net Operating Income*	Net Plant December 31	Return on Avg. Net Plant
1996	—	$10,628,201,647	—
1997	$877,000,000	10,952,004,077	8.13%
1998	781,000,000	11,531,933,757	6.95%
1999	684,000,000	15,682,448,382	4.90%
2000	642,000,000	15,805,236,141	3.46%
2001	622,000,000	15,990,835,227	3.91%
		5-Year Average	5.47%
		3-Year Average	4.09%
		2-Year Average	3.69%
		Selected =	4.50%

Return on Average Net Plant (from above)				4.50%
Rate of Return Required by Investors =				11.70%
Percent Actual Rate of Return of Investor Required Rate of Return =				38.46%
Percent Obsolescence in Existing Plant:				
100.00%	less	38.46%	=	61.54%

* NOI from Annual Supplement to CSX Corporation Annual Report (Rail), p. 3.

Explanation of Cost Approach

The basis of the cost approach used in this appraisal is original cost less depreciation. As stated in the introduction to the cost section of the report, replacement cost less deprecia-

tion and all obsolescence would approximate original cost less depreciation and obsolescence. Because of the facts set out above, we have used the original cost less depreciation as the basis of the cost approach. This cost includes road and equipment property and equipment, land, construction work in progress, materials and supplies, and leased property. The total net investment in operating railroad property of CSX Transportation Inc., on January 1, 2002, is $15,990,835,227.

A prospective purchaser of the operating property of CSX Transportation Inc. would require a market rate of return. If the adjusted net operating income is divided by the average net property investment which earned that income, the rate of return on assets can be calculated. The rate of return for the last five years has been between approximately 3.50% and 8.00%, with the highest year being 8.13% in 1997 (before the 42% Conrail purchase was completed). The latest year's rate of return is 3.91%. The five-year average rate of return was 5.47%, the three-year average rate of return was 4.09%, and the two-year average rate of return was 3.69%. We selected 4.50% as the appropriate average rate of return for use in measuring external obsolescence. This selection was based upon the most recent two years (with Conrail fully integrated) and considering general information regarding expected rates of return. If this 4.50% selected rate of return is compared with the investor required return of 11.70%, the Company's performance is 7.20% below the investor required return (11.70% - 4.50% = 7.20%). This 4.50% rate of return which is 7.20% lower than required cost of capital equates to a 61.54% external obsolescence factor (7.20% ÷ 11.70% = 61.54%).

Note: These computations have been made in accordance with the methodology presented in two authoritative textbooks quoted and discussed as follows:

The proper measurement for external (economic) obsolescence is stated by the Appraisal Institute as follows:

> Two methods can be used to measure external obsolescence. The appraiser should select the procedure that is best supported by market evidence. The appraiser can either 1) capitalize the income or rent loss attributable to the negative influence, or 2) compare sales of similar properties that are subject to the negative influence with others that are not. If pertinent sales data are abundant, the second procedure is preferred. However, an appraiser may encounter significant practical problems in attempting to account for other differences between the subject property and the comparable properties. Care should be exercised when this method is used.[14]

The computations made to derive the external obsolescence in this appraisal report relate to method number one (1) just quoted. These computations recognize that CSX Transportation Inc. has not earned its market required cost of capital on its total net investment in plant and equipment. (The primary causes for this below-market rate of return on all property are the intense level of competition and the high costs of doing business.)

The need for measuring obsolescence by the use of income data is discussed in *The Handbook of Advanced Business Valuation* as follows:

> A properly applied cost approach would have to consider both the functional and economic obsolescence of the assets. Both of these forms of obsolescence are measurable for the most part through an investigation of the earning capacity of the Facility....The analyst began with the income approach. This is because certain elements of

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[14] Appraisal Institute, *The Appraisal of Real Estate*, 10th ed., (Chicago: Appraisal Institute, 1992), 358.

> the income approach, such as rates of return, would also be needed in the application of the cost approach.[15]

This topic is further expounded upon in *Capitalization Theory and Techniques* as follows:

> The entire valuation process is comprised of integrated, interrelated, and inseparable procedures with the common objective of arriving at a convincing and reliable estimate of value. Although the approaches may be documented and explained on different pages of the appraisal report, they are rarely truly independent and unrelated. At times, the three approaches (if used) are so intertwined that some appraisers prefer the "one approach" concept and do not subscribe to the custom of separate presentations of the sales comparison approach, the income capitalization approach, and the cost approach.[16]

Specific treatment of the appraisal principles and techniques applicable to railroads and public utilities and businesses in the measurement of external obsolescence is further illustrated in the appraisal textbook entitled *The Valuation of Real Estate* as quoted on the following page.

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[15] Reilly, Robert F. and Schweihs, Robert P., *The Handbook of Advanced Business Valuation*, (New York: McGraw-Hill, 2000), 257.

[16] Charles B. Akerson, MAI, *Capitalization Theory and Techniques*, 2nd ed. (Chicago: Appraisal Institute, 2000), p. 6.

Most railroads and practically all public utilities incur a third and often severe loss in value due to external obsolescence. This loss in value, as demonstrated below under the cost approach to value, is caused by the difference in the *rate* of return allowed by regulatory agencies and the rate of return that the investment market indicates as competitive to attract a willing, able, and informed purchaser (investor).

The application of the cost approach to value is illustrated as follows:

Book value of gross plant		$250,500,250
Current assets		15,220,150
Construction work in progress		45,300,000
Materials and supplies		12,420,800
Total value of gross plant in operation		$323,441,200
Add: Depreciated value of leased properties		85,358,300
Total book value before depreciation		$408,799,500
Less: Accrued depreciation		
Physical - per book	$115,420,000	
External = 17.4% of depreciated plant value* or 0.174 x $293,379,500 =	51,048,033	
Total depreciation		$166,468,033
Value via cost approach		$242,331,467

* Depreciated plant value is difference between total book value — before depreciation of $408,799,500 and accrued physical book depreciation of $115,420,000 or $408,799,500 - $115,420,000 = $293,379,500

External depreciation is calculated as follows:

Market rate of capitalization	11.5%
Allowed rate of return	9.5%
Loss in earnings	2.0%

Loss in earnings of 2% ÷ market rate of 11.5% = 17.4% external obsolescence.[17]

[17] Alfred A. Ring and James H. Boykin, *The Valuation of Real Estate*, 3rd ed., (Englewood Cliffs, NJ: Prentice-Hall, 1986), 424.

The use of any other method of measuring obsolescence in the appraisal of the operating properties of railroad operating properties (other than the two methods quoted from the textbook of the Appraisal Institute) is not in agreement with generally accepted appraisal principles established by recognized appraisal authorities. By using the recognized appraisal principles for the measurement of obsolescence, the appraiser can generate a meaningful opinion of market value by the cost approach.

Not only is it necessary to adjust for external obsolescence in the appraisal process, it is unethical in practice to fail to investigate and take into account the loss in value resulting from external obsolescence. The following statement is from the *Uniform Standards of Professional Appraisal Practice* of the Appraisal Foundation.

> This guideline also requires the appraiser to investigate and take into account not only that loss of value that results from deterioration due to age but also loss of value due to functional and economic obsolescence. Economic obsolescence is a major consideration when assets are considered as parts of a going concern.[18]

Based upon the recognized and generally accepted methodology for the measurement of external obsolescence in the appraisal of railroad property as quoted above, the operating railroad property and equipment of CSX Transportation Inc. suffers an additional amount of external obsolescence of 61.54% due to the property's inability to earn a market rate of return currently. The cause of this inability to earn a market rate of return is primarily from external competitive, economic, and governmental sources. To adjust for external obsolescence an additional amount of $9,840,759,999

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[18] Appraisal Standards Board, *Uniform Standards of Professional Appraisal Practice*, (Washington, DC: Appraisal Foundation, 1992), S.R. 9-4(b), 43.

($15,990,835,227 x 61.54%) was deducted from the existing railroad property, plant and equipment. This computation results in my opinion of value by the cost approach of $6,150,075,228.

Thus, the indicated market value by the cost approach for CSX Transportation Inc. as of January 1, 2002, when rounded, was $6,150,000,000.

The Income Approach

The income approach is based primarily on the principle of anticipation and involves converting dollars of expected future income into present value. The execution of the income approach involves the selection of the appropriate capitalization method, estimation of the expected income, and estimation of a proper capitalization rate which matches the income to be capitalized. The basic income formula is shown in the box to the right.

$$Value = \frac{Income}{Rate}$$

Income-producing property is typically purchased for investment purposes, and the projected net income stream is the critical factor affecting its market value. An investor purchasing income-producing property is in effect trading a sum of present dollars for the right to a stream of future dollars. There is a relationship between the two, and the connecting link is the process of capitalization. Because future dollars are worth less than present dollars, the anticipated future dollars are discounted to a present worth on some basis that reflects the risk and the waiting time involved.

The income approach, which is related to investor thinking and motivation, is a basic tool for the valuation of income-producing property. It is based on the principle of anticipation reflected in the definition of value as the present worth of all the rights to future benefits accruing to ownership. These future benefits consist of some pattern of annual net income to the property.

The income approach is practical only when an income stream attributable to the property can be estimated. This income estimate may be developed and supported by comparisons with similar properties under similar circumstances

or based on a projection of a combination of historical data and current events leading to expectations for the future.

The income approach is one of the three approaches to value. The three approaches to value are not independent and unrelated to each other. It may be necessary to use elements of one approach in some portions of another approach. This is a natural part of the valuation process. Regarding the income approach the Appraisal Institute states:

> The income capitalization approach is one of three traditional approaches that an appraiser may use in the valuation process. However, it is not an independent system of valuation that is unrelated to the other approaches. The valuation process as a whole is composed of integrated, interrelated, and inseparable techniques and procedures designed to produce a convincing and reliable estimate of value, usually market value. The analysis of cost and sales data is often an integral part of the income capitalization approach, but capitalization techniques may be frequently employed in the cost and sales comparison approaches as well. For example, capitalization techniques are commonly used to analyze and adjust sales data in the sales comparison approach; in the cost approach, obsolescence is often measured by capitalizing an estimated rent loss.[19]

In the income approach for the operating property of a railroad company the present value of the future benefits of property ownership is estimated. This approach is particularly applicable to income producing companies where profit is the main motive for property ownership.

The typical investor's objective in any investment is to ultimately receive more than the amount invested. The inves-

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[19] Appraisal Institute, *The Appraisal of Real Estate*, 10th ed., (Chicago: Appraisal Institute, 1992), 409.

tor thus wants a complete return *of* all capital invested and in addition a fair return *on* the capital invested. Thus, the investor expects to completely recoup his investment and be fairly compensated for the use of his capital. The return *of* capital is usually referred to as the recapture of the initial capital investment. The return *on* capital is usually referred to as the compensation an investor receives for the use of his capital until it is recaptured.

In this appraisal we have used yield capitalization as the technique to produce the income approach to value indicator.

Yield Capitalization

Yield capitalization is a method of converting a series of income flows (called cash flows) into present value by discounting the expected future benefits at an appropriate discount rate (synonymous with the property's *overall yield rate* or *cost of capital*).

> To perform yield capitalization, an appraiser l) selects an appropriate holding period; 2) forecasts all future cash flows or cash flow patterns; 3) chooses an appropriate yield, or discount rate; and 4) converts future benefits into present value by discounting each annual future benefit or by developing an overall rate that reflects the income pattern, value change, and yield rate. The application of capitalization rates that reflect an appropriate yield rate, the use of present value factors, and discounted cash flow analysis are all yield capitalization procedures.[20]

Thus, the appraiser performs yield capitalization by either 1) discounting the cash flow to its present value for the duration of the income, or 2) capitalizing the appropriate income at an overall capitalization rate, which represents the income pattern, value change, and yield rate.

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[20] *Ibid.*, 483.

Upon projecting the amount, timing, and duration of the cash flows to the property being appraised, the appraiser must identify the pattern that the cash flow is expected to follow during the holding period. Those patterns are either a variable annuity, level annuity, increasing annuity, or decreasing annuity. For a level annuity where a property is expected to generate a level cash flow for a finite period of time and maintain its value during that period, the property can be valued with capitalization in perpetuity by dividing the periodic income by the appropriate discount rate. In this model the discount rate and the overall capitalization rate are the same.[21]

When the net income consists of a fixed amount that represents the return of capital (depreciation expense) plus a declining amount representing the return on the capital remaining in the investment, classic straight-line capitalization can be used to value the property.[22] In this model, as with the level perpetuity, the discount rate and the overall capitalization rate are the same.

If the cash flow pattern is expected to be in the form of a variable annuity each individual income flow will be discounted into an indication of present worth at the appropriate discount rate for the holding period. Further, the appraiser discounts any remaining value in the investment at the end of the holding period and adds the total present worth of the variable cash flows to the present worth of the future value at the end of the holding period. The total represents the present worth of the total property.

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[21] *Ibid.*, 490.

[22] *Ibid.*, 496.

The application of the DCF model for a variable annuity can be accomplished using the following formula.

$$Value = \frac{I_1}{(1+r)^1} + \frac{I_2}{(1+r)^2} + \frac{I_3}{(1+r)^3} + \ldots + \frac{I_n}{(1+r)^n}$$

In this formula, *I* equals income or cash flow in periods 1 through n, and *r* equals the discount rate. Where income has the characteristics of a perpetuity or of a classic straight line capitalization model, the universal capitalization formula, *Value = Income ÷ Rate*, can be used. In this case the overall capitalization rate will equal the discount rate.

Estimation of Income to Capitalize

The income level capitalized in yield capitalization is usually called cash flow. In fact, Dr. William Kinnard, MAI clarifies this in his appraisal textbook.

> "All of the annual 'income' figures used in appraising income-producing properties are *cash flows* rather than accrual accounting incomes."[23]

Cash flow can be defined in a number of ways, however for appraisal purposes it generally consists of income necessary to satisfy the cost of capital plus depreciation expense. Commercial and general appraisers recognize this level of income as simply *net operating income*. Railroad and utility appraisers know that the definition of "net operating income" for railroads, public utilities and commercial properties is different in one important aspect. For railroads and public utilities the level of income reported as "net operating income" is only that income available to pay the railroad or utility's cost of capital, while for commercial properties "net operating income" includes not only the level of income available for

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[23] William N. Kinnard, Jr., *Income Property Valuation*, (Lexington: Heath Lexington Books, 1982), 70.

debt and equity, but also the income to recapture a portion of the wasting asset (*otherwise known as depreciation expense*). For this appraisal of CSXT's operating property we have defined net operating income similar to the definition used by railroads and public utilities.

In general commercial appraisals cash flow is typically defined as simply net operating income, which is the income available for debt and equity plus the depreciation expense. For an illustration of this type of analysis, refer to *The Appraisal of Real Estate*, 11th edition, page 564.

For unit concept appraisals cash flow is often defined as net operating income (defined as the income available to pay the cost of capital) plus depreciation expense and the current portion of deferred income taxes. This definition of cash flow is sometimes referred to as *gross cash flow* because there is no deduction for capital expenditures to keep the unit operating, Thus, this cash flow model will have a limited life duration. In other words, gross cash flows cannot continue indefinitely without significant new investment to keep the railroad operations ongoing.

Another variation of this same general definition of cash flow is called *net cash flow*, which is the gross cash flow less capital expenditures. Some refer to this as gross revenue less all cash expenses except interest expense. For the appraisal of railroad operating properties where it is assumed that the amount of capital reinvestment is equal to the depreciation expense, *net cash flow* can be defined simply as net operating income. (*Note: For the typical railroad such as CSXT, capital expenditures will almost always exceed the annual depreciation expense resulting in a growing capital asset base. However, for the ad valorem tax appraisal of the typical railroad we can conservatively assume that the capital expenditures equal the depreciation expense resulting in a static level of investment indefinitely. The basis for this reasoning is that we are only appraising the existing level of assets at the date*

of the appraisal for property tax purposes.) For the appraisal of a railroad operating property as a going concern, net cash flow may be the easiest level of income to work with. To estimate the net cash flow for railroad operating properties in yield capitalization generally the same methods used to estimate net operating income may be employed.

It is critical to remember, using net operating income as a surrogate for net cash flows implies that there will be no growth in railroad properties as a result of capital expenditures in excess of the annual level of depreciation expense. While this may seem at odds with what is actually happening with CSXT's operating properties, it is irrelevant to the appraisal problem. The appraiser may appraise the current level of operating property by assuming no growth or decline in overall net investment. Assuming that all new capital investment simply earns its cost of capital, new growth in assets in the future will not impact the current value of the existing assets subject to appraisal. From an appraisal standpoint, it does not matter. One may simply estimate the market value of the current level of assets assuming a level income for the unit discounted at the current cost of capital or by assuming an increasing income (propelled by reinvesting in more assets than are currently in existence at the appraisal date). If the appraiser uses a growing level of income for discounting to current market value, it is appropriate to use net cash flow which will typically be lower than the current net operating income and the appropriate discount rate will be the cost of capital rate less the expected growth in overall value. Either method is acceptable. [*It should be noted by the reader that for the next several years, like the last several years, CSXT is expected to have capital expenditures, which exceed depreciation expenses and would tend to lead to annual growth in the net investment base. The vast majority of the capital expenditures currently and expected for the future are to replace infrastructure assets currently in existence.*] For this appraisal we have assumed a level net

cash flow projection discounted at the cost of capital rate. Thus, we have used our estimate of expected levelized net operating income as a surrogate for net cash flow to discount.

The Capitalization Rate

The capitalization rate to use in yield capitalization is known by several different names — *cost of capital rate,* the *weighted average cost of capital,* the *discount rate,* and the *overall yield rate.* All of these terms are synonymous with the rate of return on total capital and are proper to use in yield capitalization. The Appraisal Institute defines the overall yield rate as follows:

> The *overall yield rate* (Y_o) is a rate of return on the total capital. It represents a weighted average of the equity yield rate and the mortgage yield rate.[24]

Thus, the discount rate can be estimated by the use of one of the same methods as used in direct capitalization which is the band of investment technique. The band of investment technique using the yield rates for debt and equity produces the weighted average cost of capital which is the appropriate discount rate in yield capitalization. Further, if the income in yield capitalization represents a perpetuity with no change in value or if the income has the characteristics of straight line capitalization, all of the techniques used in direct capitalization to obtain the overall capitalization rate will be valid for estimating the overall yield rate because, as discussed earlier, in those circumstances the overall capitalization rate and the overall yield rate will be equal.

Further, to derive *equity yield rates* from market information yield capitalization permits some things that would not be proper using direct capitalization. For example, appraisal texts record how it is permissible to use stocks and bonds for

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[24] *The Appraisal of Real Estate*, 10th ed., (Chicago: Appraisal Institute, 1992), 426.

determination of equity yield rates in alternative investments when appraising real estate.

> An investor may compare the expected equity yield on a real property investment with the yields on alternative investments with commensurate risk (e.g., stocks and bonds) and with a lender's yield on mortgages secured by similar real property.[25]

The Appraisal Institute goes on to state:

> To estimate equity yield rates, appraisers must do market research. This research can take many forms and may include one or more of the following analyses. . . Comparison with the equity yield rates achieved in alternative investments of comparable risk such as stocks and bonds . . .[26]

When using any capitalization method, the reliability of the income approach is dependent upon the reasonableness of the estimate of anticipated future income and the capitalization rate. The first area of concern is estimating the income to be capitalized and the quantity, quality, and duration of the income. The second area of concern is estimating a proper rate of capitalization.

The computations showing actual net operating income and a variety of averages and trends in net operating income are on the following page. In addition, the capitalization computations based on the estimated future net operating income (a liberal surrogate for the net cash flow of CSXT) and the proper capitalization rate (discount rate) are shown.

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[25] *The Appraisal of Real Estate*, 11th ed., (Chicago: Appraisal Institute, 1996), 554.

[26] *Ibid.*, 555.

CSX TRANSPORTATION, INC.
Indication of Value by Income Approach
January 1, 2002

Year	Net Operating Income*	Weighting	Product
1997	$877,000,000	1	$877,000,000
1998	781,000,000	2	1,562,000,000
1999	684,000,000	3	1,992,000,000
2000	542,000,000	4	2,168,000,000
2001	622,000,000	5	3,110,000,000
Average	$697,200,000	15	$9,709,000,000
	5-Year Weighted Average =		$647,266,667
	3-Year Weighted Average =		$602,333,333

2001 Net Operating Income	$622,000,000
2-Year Average Net Operating Income	582,000,000
5-Year Average Net Operating Income	697,200,000
5-Year Wtd. Adjusted Net Oper. Income	647,266,667
3-Year Wtd. Average Net Oper. Income	602,333,333
Discounted Least Squares Regression (DF=0.80)	571,012,312
Discounted Least Squares Regression (DF=0.60)	581,323,857

Estimated Future Net Cash Flow	$700,000,000
Discount Rate	11.70%
INDICATED VALUE BY INCOME APPROACH	$5,982,905,983
(Rounded)	$5,983,000,000

* NOI from Annual Supplement to CSX Corporation Annual Report (Rail).

Explanation of Income Approach

Determination of Net Cash Flow to be Capitalized

Our efforts to estimate the future cash flow to be derived from CSXT's properties as they existed as of the appraisal date centered primarily on projected and anticipated future net operating income estimates as a surrogate for net cash flow. As mentioned on page 33, net operating income can be considered as an estimate of net cash flow for use in yield capitalization where it is expected that the income will have the characteristics of a level perpetual income stream or the characteristics indicative of classic straight line capitalization. Straight line capitalization is appropriate when 1) recapture is based on equal annual amounts, 2) the return on investment is

expected to be a percentage of the undepreciated balance of the investment, and 3) the income is expected to decline as the property ages.

We considered income information for the last several years, economic cycles in the railroad industry, simple and weighted averages, trend analysis, and income based on projections after considering Company provided data. Our income projections were based on the income statements provided in the Supplement to the Annual Report for CSX Corporation. Upon discussions with CSX personnel we believe that the rail income data provided in this document provides us with the best indication of income data for our appraisal of CSXT. We believe the income data from the latest two years before the appraisal date provide the most meaningful income figures. This is because the Conrail operations were reflected in the results for these two years. The reported net operating income for the year ended December 31, 2001 was $622,000,000. [This is calculated by deducting the income tax expense of $121 million from the Rail Operating Income Before Fees & Special Items of $743 million.] The two-year average, five-year average, and five-year weighted average adjusted net operating incomes computed in the same manner were $582,000,000, $697,200,000, and $647,266,667 respectively.

CXST pays a fee to CSX Corp for the provision of most of its management functions. CSXT also pays a fee to CSX Technologies for the provision of all of its technology requirements. During the years leading up to December 31, 2001 those fees were broken into two portions; a portion which contained only the actual cost of providing the service (Tier 1), and the portion which represented a profit to the provider (Tier 2). When the company reports the results of its rail segment, it treats the Tier 2 portion (the profit) of both of those fees as if it were not an operating expense. This is the management view shown in the Supplemental Report to the

Annual Report for rail purposes. We have concluded that like the company we will consider future cash flows by treating only the Tier 1 portion of those fees as ordinary sustainable operating expenses.

CSXT has experienced significant volatility in the net operating income throughout its entire history, and, in fact, the entire railroad industry in general has experienced wide fluctuations in this regard. The latest two years operating results are most indicative of the current earnings capabilities of the Company because the Conrail operations are included in the rail income figures. With high fuel prices, potential economic and labor woes, and railroad industry volatility, we expect the levelized net cash flow on a going-forward basis to be in the $700,000,000 range. Our estimate of future stabilized income (net cash flow) includes a cushion to cover our expectations of future income growth, other miscellaneous income from railroad operations and any residual income adjustment for operating lease benefits. Our estimate of long-term level net cash flow takes into consideration the investment that CSXT has committed to its business, the economics of the railroad industry, and the long-time turbulent fluctuation in CSXT's operating income.

After consideration of all the factors pertinent to the estimation of future income for CSX Transportation Inc., it is believed that the property existing at the appraisal date will produce levelized net cash flow of approximately $700,000,000. Our future net cash flow estimate of $700,000,000 includes an estimate of income for construction work in progress and the impact of all operating leased property used by the Company, other miscellaneous income from railroad operations, as well as growth from the current level of earnings. We have considered the best information available from published materials provided by Company officials along with historical earnings and net cash flow projections.

Income Approach Calculation

Utilizing the income approach formula, income divided by rate equals value, we divided the estimated net operating income by the cost of capital to obtain the market value by the income approach. When the estimate of future income is capitalized at the proper discount rate of 11.70%, the indication of value by the income approach was $5,982,905,983. Thus, as of January 1, 2002 our indication of market value for the operating property of CSXT by the income approach was $5,983,000,000. Detailed explanation of the derivation of the cost of capital follows.

The Cost of Capital (Discount Rate)

The estimated cost of capital in this report for CSX Transportation Inc. as of January 1, 2002 is based on the generally accepted appraisal methodology known as the band of investment technique. The band of investment technique consists of the following steps:

1. Analyze and determine the appropriate capital structure.
2. Identify the appropriate cost for each financing band of the capital structure.
3. Weight the appropriate cost for each financing band by the relative proportion of the capital structure represented by each financing band.

The sum of the weighted costs for the financing bands represents the weighted average cost of capital. This weighted cost of capital is typically known as the discount rate in appraisal literature and the algebraic formula is shown in Figure 1.

$$K = (D \times D_r) + (E \times E_r)$$

where

K = Weighted Average Cost of Capital
D = Proportion of Debt in Capital Structure
D_r = Cost of Debt
E = Proportion of Equity in Capital Structure
E_r = Cost of Equity

Figure 1

In explaining the estimation of the cost of capital, Ibbotson Associates states:

> The cost of capital is always an expectational or forward-looking concept. While the past performance of an investment and other historical information can be a good guide and is often used to estimate the required rate of return on capital, the expectations of future events are the only factors that actually determine the cost of capital. (An investor contributes capital to a firm with the expectation that the business's future performance will provide a fair return on the investment. If past performance were the criterion most important to investors, no one would invest in startup ventures.)[27]

The cost of capital for CSX Transportation Inc. as of January 1, 2002 is estimated to be 11.72% (rounded to 11.70%) as the chart below indicates. Following the chart are explanations of the derivation of each of the component parts.

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[27] *SBBI (Stocks, Bonds, Bills and Inflation)*, 1997 Yearbook, (Chicago: Ibbotson Associates, 1997), 143.

Corp Tax Rate 38.00%				Flotation Cost Adjustment			
Capital	Portion	Cost	Product	Flot. Cost	Division	Adj Cost	Product
Debt	40.00%	8.05%	3.22%	1.00%	99.38%	8.10%	3.24%
Equity	60.00%	13.50%	8.10%	4.50%	95.50%	14.14%	8.48%
Totals	100.00 %		11.32%				11.72%

In the computations above the sum of the products obtained by multiplying the respective portions of the capital structure represented by debt and equity times their respective rates is the cost of capital rate. The use of the band of investment method with the mortgage and equity components is a very practical method which can be used in the appraisal of railroads and public utilities. It is also exactly the same method and type of calculation made by regulatory commissions when setting the authorized rate of return for those public utilities which are operating under rate of return regulation and the Surface Transportation Board when determining adequacy of revenues for railroads.

Capital Structure

Economists and appraisers measure a firm's capital structure in terms of the market values of its debt and equity because that is the best measure of the amounts of debt and equity that investors have invested in the company on a going-forward basis. Furthermore, economists and appraisers generally agree that the goal of management is to maximize the value of the firm, where the value of the firm is the sum of the market value of the firm's debt and equity. Only by measuring a firm's capital structure in terms of market values can its managers choose a financing strategy that maximizes the value of the firm.

As the operating environment of railroad companies evolves into a consistently more competitive posture, investors and analysts are finding other fundamentals changing and appraisers must acclimate appraisal procedures to those changes. Appraisers involved in the appraisal of railroads must be aware of the evolutionary processes occurring within the industry and consider their effects on the valuation process. We must rely on generally accepted appraisal principles and utilize market capital structures when estimating the cost of capital for CSX Transportation Inc.

For estimating the cost of capital for CSX Transportation Inc. it is appropriate to use the typical market capital structure for similar railroad companies. There is very little debate about this concept, however for clarity we note the following statement from Brigham and Gapenski.

> We are absolutely convinced that the procedures we recommend are correct — namely, firms should focus on market value capital structures and base their cost of capital calculations on market value weights. Because market values do change, it would be impossible to keep the actual capital structure on target at all times, but this fact in no way detracts from the validity of market value targets.[28]

It is also important to note what elements of capital comprise the makeup of the *capital structure* from an appraisal standpoint. For appraisal purposes, the capital structure consists only of long-term debt, common stock, and where appropriate, preferred stock. The capital structure should not be confused with *financial structure* or any other term used in financial literature. To understand what elements comprise the capital structure it is important to define capital structure and *financial structure*, which are defined as follows:

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[28] Eugene F. Brigham and Louis C. Gapenski, *Financial Management*, 7th ed. (New York: The Dryden Press, 1994), 599.

> CAPITAL STRUCTURE corporation's financial framework, including LONG-TERM DEBT, PREFERRED STOCK, and NET WORTH. It is distinguished from FINANCIAL STRUCTURE, which includes additional sources of capital such as short-term debt, accounts payable, and other liabilities.[29]
>
> FINANCIAL STRUCTURE makeup of the right-hand side of a company's BALANCE SHEET, which includes all the ways its assets are financed, such as trade accounts payable and short-term borrowings as well as long-term debt and ownership equity. Financial structure is distinguished from CAPITAL STRUCTURE, which includes only long-term debt and equity.[30]

It is also important to note that neither accumulated depreciation nor accumulated deferred income taxes are included in capital structure. Some appraisers have mistakenly included accumulated deferred income taxes in constructing a firm's capital structure. This is simply wrong for estimating the cost of capital and for appraisal purposes. The following quotation addresses this issue quite well:

> Since depreciation-generated funds have the same cost as the firm's WACC when retained earnings are used for the equity component, it is not necessary to consider them when estimating the WACC...Therefore, deferred taxes, like depreciation, have a cost equal to the firm's WACC using retained earnings as the equity component. Indeed, deferred taxes arise solely because a firm records a different depreciation expense on its tax books than on the books used to report income to shareholders. . . Deferred taxes are treated the same way as

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[29] John Downes and Jordan Elliot Goodman, *Dictionary of Finance and Investment Terms*, (New York: Barron's, 1985), 54.

[30] *Ibid.*, 132.

> depreciation cash flows: they are not included when estimating the firm's WACC. . . [31]

The appropriate capital structure for use in estimating CSX Transportation Inc.'s cost of capital is the expected capital structure that a typical purchaser would likely use to finance the purchase of the operating assets of the Company. Thus, an analysis of the typical market capital structure used in the railroad industry is appropriate. The market capital structure developed for CSX Transportation Inc. was calculated from information obtained from *The Value Line Investment Survey* and *Standard & Poor's Research Insight* data bases as of January 2002. The capital structure analysis was made by considering the capital structures of the several groups of companies in the railroad industry. The average and median capital structures of the Value Line railroad industry (all 10 companies with traded stock) were approximately 40% debt and 60% equity using both *Value Line* and *Standard & Poor's* data. Additionally, the capital structures of the large railroad companies (annual sales of over $2.5 billion) were approximately 40% debt and 60% equity using both *Value Line* and *Standard & Poor's* data. Our selection of a market capital structure of 40% debt and 60% equity may be considered slightly conservative, in view of the fact that CSX and Norfolk Southern have been recently involved in consolidations requiring the taking on of large amounts of long-term debt. The capital structure calculations are shown on the following pages.

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[31] Eugene F. Brigham and Louis C. Gapenski, *Financial Management*, 7th ed. (New York: The Dryden Press, 1994), 368-369.

Capital Structure - January 1, 2002
Value Line Railroad Industry (All) - Value Line Data

Company Name	Ticker	LTD%	PS%	CS%
Burlington Northern	BNI	37.53%	0.00%	62.47%
CSX Corp.	CSX	42.82%	0.00%	57.18%
Florida East Coast	FLA	22.71%	0.00%	77.29%
Kansas City South'n	KSU	45.49%	0.43%	54.08%
Norfolk Southern	NSC	49.71%	0.00%	50.29%
Pioneer Railcorp	PRRR	69.12%	0.00%	30.88%
Providence & Worcester R R	PWX	0.00%	0.00%	100.00%
RailAmerica Inc.	RRA	56.44%	0.00%	43.56%
Union Pacific	UNP	40.61%	0.00%	59.39%
Genesee & Wyo Inc	GNWR	27.28%	6.04%	66.68%
	Average	39.17%	0.65%	60.18%
	Median	41.71%	0.00%	58.29%

Source: Value Line Data Base, January 2002.

Capital Structure - January 1, 2002
Value Line Railroad Industry (Large) - VL Data

Company Name	Ticker	LTD%	PS%	CS%
Burlington Northern	BNI	37.53%	0.00%	62.47%
CSX Corp.	CSX	42.82%	0.00%	57.18%
Norfolk Southern	NSC	49.71%	0.00%	50.29%
Union Pacific	UNP	40.61%	0.00%	59.39%
	Average	42.67%	0.00%	57.33%
	Median	41.71%	0.00%	58.29%

Source: Value Line Data Base, January 2002.

Capital Structure - January 1, 2002
Value Line Railroad Industry (All) - S&P Data

Burlington Northern Santa Fe	BNI	36.29%	0.00%	63.71%
CSX Corp	CSX	43.10%	0.00%	56.90%
Florida East Coast Inds	FLA	22.78%	0.00%	77.22%
Genesee & Wyoming Inc -Cl A	GNWR	25.74%	5.68%	68.58%
Kansas City Southern Inds	KSU	43.35%	0.41%	56.24%
Norfolk Southern Corp	NSC	49.99%	0.00%	50.01%
Pioneer Railcorp -Cl A	PRRR	69.25%	0.00%	30.75%
Providence And Worcester Rr	PWX	0.00%	0.11%	99.89%
RailAmerica Inc	RRA	55.89%	0.00%	44.11%
Union Pacific Corp	UNP	40.67%	0.00%	59.33%
	Average	38.71%	0.62%	60.67%
	Median	41.89%	0.00%	58.12%

Source: S&P Research Insight CD Rom, January 2002.

Capital Structure - January 1, 2002
Value Line Railroad Industry (Large) - S&P Data

Burlington Northern Santa Fe	BNI	36.29%	0.00%	63.71%
CSX Corp	CSX	43.10%	0.00%	56.90%
Norfolk Southern Corp	NSC	49.99%	0.00%	50.01%
Union Pacific Corp	UNP	40.67%	0.00%	59.33%
	Average	42.51%	0.00%	57.49%
	Median	41.89%	0.00%	58.12%

Source: S&P Research Insight CD Rom, January 2002.

Cost of Debt

The expected return on debt, or the cost of debt capital (D_r) is the rate that investors would incur when financing the purchase of the operating assets of CSX Transportation Inc. It is the appropriate debt rate for the cost of capital and is relatively simple to estimate. Unlike the cost of equity, the required return on debt is directly observable in the market. It is best approximated by the current yield-to-maturity (yield) on the applicable debt. Often an average of recent yields is also used. The yield exemplifies the market's expectation of future returns. If the market's expectations of future debt returns

were different from those implicit in the price, the market price of the debt would be bid up or down so that the market's expectations were reflected in the price.[32]

From information in *Mergent's Bond Record* (January, 2002), we found the *Mergent's* bond rating to be *Baa2* for CSX Corporation.[33] We also found the *Standard & Poor's* long-term debt rating for CSX Corporation to be *BBB* as of January 1, 2002. *Mergent's Bond Record* reports Utility Bond Yields for "Baa" rated debt to be *8.27%*, Corporate Bond Yields for "Baa" rated debt to be *8.05%*, and Industrial Bond Yields for "Baa" rated debt to be *7.82%* at the end of December 2001. From this information we determined the appropriate cost of debt capital for CSX Transportation Inc. to be *8.05%* as of January 1, 2002.

Cost of Equity

In estimating the cost of equity capital, several methods are employed. The market cost of equity is often considered to be the most difficult part of computing the cost of capital because it relies on interpretation of projections by market analysts as well as the projections of the equity models used by the appraiser. The market cost of equity is equal to the *expected* rate of return for a company's equity. There are several methods used to estimate the cost of equity capital. The most common methods are the discounted cash flow method (DCF), the risk premium method (RP), and the capital asset pricing model (CAPM).

All estimates of the cost of equity rates fall into one of two classes. They are either (1) add-ons to an interest rate, or (2) ratios of return to investment. Add-on estimates of the

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[32] Eugene F. Brigham and Louis C. Gapenski, *Financial Management*, 7th ed. (New York: The Dryden Press, 1994), 147.

[33] We also noted that *Mergent Bond Record* reports Louisville & Nashville Railroad (one of the predecessors to the subject company) bonds due in 2003 are rated Baa1.

cost of equity capital include RP and the CAPM. The DCF method is a ratio of return to investment. After computing the cost of equity by the DCF, RP, and CAPM methods, the data was analyzed and reconciled to obtain the cost of equity capital of 13.50% prior to adjustment for flotation costs. This equity rate was determined after studying and analyzing much data, some of which is included in the addendum of this report. In considering this information we were aware that more risk is involved with the equity position than the debt position, thereby demanding a higher return for equity than debt. We will discuss the calculations employed in each method.

DCF Method

The discounted cash flow method of estimating the cost of equity is based on the formula shown in Figure 2. Our computations using the DCF method are based upon information from the *Standard and Poor's Research Insight* database, *Institutional Brokers Estimate System* (IBES) and the *Value Line Investment Survey* database. We began our analysis by screening the Standard and Poor's database for com-panies with approximately equal risk to the risk of CSX Transportation Inc. Further, we performed additional DCF analyses on two other groups of companies, all *Value Line* railroads and the Value Line large railroads (annual sales over $2.5 billion). We used two sets of growth estimates for all of the groups of companies. The growth estimates considered were provided by the Institutional Brokers Estimate System (IBES) and the *Value Line Investment Survey.*[34] From these analysts' projections we calculated DCF indicators on all groupings and calculated a simple average and a median of the indicators. We believe the appropriate cost of equity for

[34] The Institutional Brokers Estimate System (IBES) is a database provided through *Standard & Poor's Research Insight* of earnings expectations obtained from more than 3,500 security analysts from over 300 contributing firms.

CSX Transportation Inc. by the DCF method is 13.75% as of January 1, 2002.

$$K_e = \frac{D_1}{P_0} + g$$

where

K_e = *Cost of equity*
D_1 = *Expected Dividend in year* 1
P_0 = *Current price of stock*
g = *Growth in dividends*

Figure 2

Risk Premium Method

The risk premium method is a standard method of estimating the cost of equity (K_e) based on the formula in Figure 3. This method sums two elements of risk — a risk free rate, which is the price of time (the reward for deferring consumption and for not exposing funds to risk), and a risk premium, which is the additional reward for assuming risk. The nominal risk free rate includes the real risk free rate and an inflation premium. The risk premium includes an interest rate risk, business risk, financial risk, and liquidity risk. All of these elements are included when calculating equity cost by the risk premium method.

$$K_e = R_f + R_p$$

where

K_e = *Cost of equity*
R_f = *Risk free rate*
R_p = *Risk premium*

Figure 3

Our risk premium calculations included computations for two categories of risk premium indicators — general indicators and indicators by the same groups used in our DCF analysis. Our risk premiums were derived from the 2002 edition of *Stocks, Bonds, Bills and Inflation* (SBBI), published by Ibbotson Associates. The SBBI risk premium was cross-checked for reasonableness by information from *Value Line*.[35] Our relevant current 'safe rates' for the general indica-

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[35] In an effort to check the long-term risk premium of 7.4% from SBBI published by Ibbotson Associates, Inc., we performed our own calculations to confirm or deny the reasonableness of this figure. The SBBI risk premium figure is supported by our own calculations of risk premium by using the CAPM formula in Figure A. From *Value Line* we know the market average return on all the stocks in their database is 14.18% and that the 5-year beta is 0.89 for the full database (see statistics for full database, *Value Line* CD ROM, January 2002). Further, we know the long-term treasury bond rate is 5.86% at January 1, 2002. Therefore, we can substitute all the known elements into the CAPM formula and solve for RP as shown in Figure B. The result of this calculation is a risk premium indicator of 9.35%, which more than supports the SBBI long-term government bond risk premium of 7.4%.

$$K_e = R_f + \beta(R_p)$$

Figure A

Solve for R_p

$$R_p = \frac{K_e - R_f}{\beta}$$

$$R_p = \frac{0.1418 - 0.0586}{0.89}$$

$$R_p = 0.0935$$

Figure B

tors were derived from the sources footnoted below.[36] The 'safe rates' used for each company within the company groupings were the average yields to maturity for the company quoted in *Mergent's Bond Record* (January, 2002). The average yield to maturity for each company's bonds was added to the SBBI corporate bond risk premium to obtain an individual estimate for each company in the group. Thus, the risk premium indicators for the individual groups are specific for each company within the group and, thus, as individualized as possible for each company.

The range for all calculations using the risk premium method indicates the cost of equity to be between 10.5% and 13.4% for the general indicators and between 13.73% and 14.27% for the risk premium indicators by company groupings.

As with the DCF analysis, we calculated the simple average and median for each of the groupings of companies identified earlier. We believe the appropriate cost of equity for CSX Transportation Inc. by the risk premium method is 13.75% as of January 1, 2002. A summary of the risk premium indicators and the supporting data is in the Addendum Section.

Capital Asset Pricing Model

The capital asset pricing model (CAPM) is a generally accepted method of estimating the cost of equity (K_e) based on the formula shown in Figure 4. The CAPM method is much like the risk premium method, however the risk premium is adjusted by beta before it is added to the appropriate risk level. The two elements of risk are a risk free rate, which is the price of time (the reward for postponing consumption and for not exposing funds to risk), and a risk premium,

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[36] Ibbotson & Associates, 2002 SBBI & Risk Premia over Time Report 2002 and the Federal Reserve, January 2, 2002.

which is the additional compensation for assuming risk. The nominal risk free rate includes the real risk free rate and an inflation premium. The risk premium includes an interest rate risk, business risk, financial risk, and liquidity risk. All of these elements are accounted for when we calculated the cost of equity using the CAPM method.

$$K_e = R_f + \beta R_p$$

where

K_e = *Cost of equity*
R_f = *Risk free rate*
β = *Beta*
R_p = *Risk premium*

Figure 4

Our CAPM calculations included computations for the same groups used in our DCF analysis. Our 'safe rates' for the CAPM calculations were derived as described in the risk premium method discussed earlier. Our beta estimate was based on observing the average and median *Value Line* betas from the large railroad companies which are believed to be most similar in operating characteristics and business and financial risk to the subject railroad. The average and median betas for this group and are shown in Figure 5. Our risk premiums were derived from the 2002 edition of SBBI. Finally, we calculated a forward-looking (*Ex Ante*) CAPM indicator by deriving an expected risk premium from the S&P 500 companies. The *ex ante* CAPM indicator is a good check on the reliability of the standard CAPM because it is forward looking.

Group of Companies	Avg. Beta	Med. Beta
VL Large Railroads	1.00	1.00

Figure 5

All prospective investment in railroad companies is based on an expectation of future benefits. This is consistent with the fundamental principle underlying the income approach which is the principle of anticipation. In order to perform the *ex ante* CAPM indicator we derived the expected cost of equity for the companies making up the S&P 500 (which are expected to pay dividends). We developed the weighted average (weighted by market value) for the S&P 500, which was 14.76%. We believe this market weighted average is appropriate because the monthly fundamental beta is estimated based upon the sensitivity of a company's stock price to the overall fluctuation in the Standard & Poor's 500 (S&P 500) Index Price (with the S&P 500 being the surrogate for the market in general). The market weighted average gives most weight to the highest market value stocks and is a very good indicator of the central tendency of the overall market cost of capital.

The general CAPM indicators, using the risk premium from SBBI published by Ibbotson Associates, Inc. and our representative railroad industry beta of 1.00, indicates a cost of equity capital of approximately 13.00% (giving the most consideration to the long-term government bond indicator). The company specific CAPM indicators computed and published by *Standard & Poor's Research Insight* uses the S&P beta for each company we have listed in the study and indicates a cost of equity for of approximately 11.15%.[37] These indicators are *ex post* or based on historical facts. Again, to help determine the reasonableness of these general and specific historical indicators we also computed an *ex ante* or forward-looking CAPM indicator. The ex ante CAPM was 14.76%.

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[37] *The Standard & Poor's* Capital Asset Pricing Model (CAPM) is computed independently by *Standard & Poor's* as a part of their *Research Insight* service and is a method of determining the expected rate of return for an asset at a given level of risk.

Based upon the analysis presented and considering all the relevant facts we believe the appropriate cost of equity capital indicated by the CAPM method is 13.25% as of January 1, 2002 for CSX Transportation Inc. A summary of the CAPM indicators and the supporting data can be found in the addendum. After determining a proper rate for both debt and equity we utilized the band of investment technique to calculate an indicated capitalization rate of 11.32% before adjustment for flotation costs.

Flotation Cost Adjustment

Flotation costs are the costs associated with issuing debt and equity. They are made up of several kinds of costs including underwriter's fees, legal expenses, cost of preparing the prospectus, etc. Flotation costs can be accounted for either by amortizing the cost (reducing the cash flow to discount), or by including them in the cost of capital. Many studies have been made regarding the amount of flotation costs for debt and equity capital.[38]

All of these studies essentially reach the conclusion that a flotation cost adjustment must be made when estimating the cost of capital (even when no additional securities are expected to be issued). The following illustration is quoted by Roger A. Morin, PhD, *Regulatory Finance: Utilities' Cost of Capital,* (Arlington, VA: Public Utilities Reports, Inc., 1994), p. 170.] and fully addresses this issue.

> Brigham, Aberwald, and Gapenski (1985) performed an excellent analysis regarding the need for a flotation cost adjustment. The following illustration adapted from

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[38] See Brigham and Gapenski, *Financial Management Theory and Practice*, 7th ed., (Dryden Press: New York), 869., Richard H. Pettway, "A Note on the Flotation Costs of New Equity Capital Issues of Electric Companies," *Public Utilities Fortnightly*, March 18, 1982, and Jay R. Ritter, "The Costs of Going Public," *Journal of Financial Economics*, December 1987.

Brigham, Aberwald, and Gapenski (1985) shows that: (1) even if no further stock issues are contemplated, the flotation adjustment is still permanently required to keep shareholders whole, and (2) flotation costs are only recovered if the rate of return is applied to total equity, including retained earnings, in all future years, even if no future financing is contemplated.

The flotation cost adjustment process is shown here in Tables 6-1 through 6-3 using illustrative market data.

The assumptions used in the computation are shown in Table 1. The stock is selling in the market for $25, and investors expect the firm to pay a dividend of $2.25, which will grow at a rate of 5% thereafter. The traditional DCF cost of equity is thus k = D/P + g = 2.25/25 +.05 = 14%, or $3.50 in the first year. Nine percent of the 14%, or $2.25, will come from dividends, so that the remaining 5%, or $1.25, must then come from capital gains. To get a capital gain of $1.25 from $1.188 of retained earnings, the earnings retained must clearly earn more than 14%. Therefore, if the firm sells me a share of stock incurring a flotation cost of 5%, the traditional DCF cost of equity adjusted for flotation cost is thus ROE = D/P(1-f) + g =.09 /.95 +.05 = 14.47%

TABLE 6-1
ASSUMPTIONS

Issue Price =	$25.00
Flotation Cost =	5.00%
Dividend Yield =	9.00%
Growth =	5.00%
Equity Return = (D/P + g)	14.00
Allowed Return on Equity = (D/P(1 -f) + g)	14.47%

Table 6-2

1	$23.75	$0.00	$23.75	$25.00	1.0526	$3.44	$2.25	65.45%
2	23.75	1.19	24.94	26.25	1.0526	3.61	2.36	65.45%
3	23.75	2.43	26.18	27.56	1.0526	3.79	2.48	65.45%
4	23.75	3.74	27.49	28.94	1.0526	3.98	2.60	65.45%
5	23.75	5.12	28.87	30.39	1.0526	4.18	2.73	65.45%
6	23.75	6.56	30.31	31.91	1.0526	4.39	2.87	65.45%
7	23.75	8.08	31.83	33.50	1.0526	4.61	3.02	65.45%
8	23.75	9.67	33.42	35.18	1.0526	4.84	3.17	65.45%
9	23.75	11.34	35.09	36.94	1.0526	5.08	3.32	65.45%
10	23.75	13.09	36.84	38.78	1.0526	5.33	3.49	65.45%
		Growth(%) =	5.00	5.00		5.00	5.00	

Table 6-2 above demonstrates that only if the company is allowed to earn 14.47% on total equity (Column 3) will investors earn their cost of equity of 14%. Column 1 shows the initial common stock account, while Column 2 shows the cumulative retained earnings balance, starting at zero, and steadily increasing from the retention of earnings. Total equity in Column 3 is the sum of common stock capital and retained earnings. The stock price in Column 4 is obtained from the seminal DCF formula: D /(k - g). Earnings per share in Column 6 is simply the allowed return of *14.47%* times the total common equity base. Dividends start at $2.25 and grow at 5% thereafter, which they must do if investors are to earn a 14% return. The dividend payout ratio remains constant, as per the assumption of the DCF model. All quantities, stock price, book value, earnings, and dividends grow at a 5% rate.

Only if the company is allowed to earn 14.47% on equity do investors earn 14%. For example, if the company is allowed only 14%, the stock price drops from $26.25 to $26.13 in the second year, inflicting a loss on shareholders. This is shown in *Table 3*. The growth rate drops from 5% to 4.53%. Thus, investors only earn 9% + 4.53% = 13.53% on their investment. *It is noteworthy that the adjustment is always required each and every*

year, whether or not new stock issues are sold in the future, and that the allowed return on equity must be earned on total equity, including retained earnings, for investors to earn the cost of equity.[39]

Table 6-3

Year	Book Value	Earnings	Retained Equity	Total Stock Equity	Market/Book Ratio	EPS	DPS	Payout
1	$23.75	$0.00	$23.75	$25.00	1.0526	$3.33	$2.25	67.67%
2	23.75	1.08	24.83	26.13	1.0526	3.48	2.35	67.67%
3	23.75	2.20	25.95	27.31	1.0526	3.63	2.46	67.67%
4	23.75	3.37	27.12	28.55	1.0526	3.80	2.57	67.67%
5	23.75	4.60	28.35	29.84	1.0526	3.97	2.69	67.67%
6	23.75	5.88	29.63	31.19	1.0526	4.15	2.81	67.67%
7	23.75	7.23	30.98	32.61	1.0526	4.34	2.93	67.67%
8	23.75	8.63	32.38	34.08	1.0526	4.53	3.07	67.67%
9	23.75	10.09	33.84	35.62	1.0526	4.74	3.21	67.67%
10	23.75	11.62	35.37	37.24	1.0526	4.95	3.35	67.67%
		Growth(%) =	4.53	4.53		4.53	4.53	

Additionally, Dr. Roger Ibbotson refers to flotation cost in his book, Stocks, Bonds, Bills and Inflation, when he discusses the cost of capital. He states the following:

> Although the cost of capital estimation techniques set forth later in this book are applicable to rate setting, certain adjustments may be necessary. One such adjustment is for flotation costs (amounts that must be paid to underwriters by the issuer to attract and retain capital).[40]

The flotation costs associated with debt for large issues conservatively are approximately 1 to 3%. For relatively large issues of equity, the flotation costs range from a low of 2% to as much as 6%. The amount of flotation costs used in determination of the cost of capital are 1.00% for debt and 4.50% for equity. These figures are supported by information from

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[39] Roger A. Morin, PhD, *Regulatory Finance: Utilities' Cost of Capital*, (Arlington, VA: Public Utilities Reports, Inc., 1994), p. 170. (emphasis added)

[40] *Stocks, Bonds, Bills and Inflation: 1999 Yearbook, Valuation Edition* (Chicago: Ibbotson & Associates, Inc., 1999), p. 34.

the railroad industry and the February 2002 issue of *Public Utility Finance Tracker*.

The Sales Comparison Approach to Value

In the appraisal field it is well recognized that cash equivalent prices, which are the result of arms-length trading between reasonably informed buyers and sellers — under no coercion and under no unusual time limitations or pressures — are the best evidences of value. Indeed, such prices are value.

There is a very limited amount of actual sales data to be used as an evidence of value for the valuation of major going-concern business enterprises such as railroads and public utilities. Regarding this phenomenon Mr. William R. Field, an economic analyst with H. Zinder & Associates, Inc. states the following.

> Obviously, it is impossible to adjust prices which are available on residential and farm property and use such adjusted prices to properly determine market value for a huge business enterprise such as, for example, a pipeline. Indeed, even sales prices for other business enterprises, and even other pipelines, might not be good indications of value for a particular, and usually unique, pipeline. Equating differences among or between business enterprises, even within the same general business field, requires so many subjective adjustments that the sales comparison approach is just not available as a practical matter in the field of public utility valuation.[41]

Because of the lack of comparable sales price data in the railroad and public utility field, appraisers have had to search for proxies or substitutes for such indicators of value. To some appraisers, it appears logical that since there seldom are available objective market evidences of value for business properties, the next best alternative is the market price of

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[41] Field, William R., "Market Value of Stock and Debt as Evidence of Market Value," *National Tax Journal*, June, 1972, 243.

the securities of the enterprise owning the properties. It is assumed that the market value of the securities is the market value of the assets of the business enterprise. Thus the stock and debt approach emerges as a substitute for the traditional sales comparison approach.

It is noteworthy to recognize that during any given day, month, or year, many of the outstanding securities of a particular enterprise are seldom involved in transactions. In fact, some companies have securities which are never publicly traded. Even when a company has common stock actively traded by the public, the portion traded in any time period is a relatively small part of the total shares outstanding. Even when security price data are available, an important question is, does such security price data, especially based on relatively small unit transactions, represent the value of the enterprise? Many financial experts believe the motivation and expectations of the investors, each separately buying insignificant quantities of the outstanding stocks, are geared very much to their individual portfolio and marketability needs. They do not want to own and operate the enterprise; they want to own the stock and all the rights which are attached to such ownership.

One who advocates the stock and debt approach as the primary evidence of value for the underlying assets should consider that the stock ticker too often registers an aggregate valuation for enterprises that is totally unrelated to what a normal appraisal of the underlying business would produce.[42]

> It was little short of nonsense for the stock market to say in 1937 that General Electric Company was worth $1,870,000,000 and almost precisely a year later that it was worth only $784,000,000. Certainly nothing had happened. . . To speak of these prices as representing

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[42] Louis Lowenstein, *What's Wrong With Wall Street* (New York: Addison-Wesley Publishing Co., Inc., 1988), 43.

> "investment values" or the "appraisal of investors" is to do violence either to the English language or to common sense, or both.[43]

Another disquieting factor is that the stock market is largely a market of secondary transactions, a market of derived demands. It is very unlike the wheat market, for example, where the ultimate purchasers do not make their purchases with a view to resale but rather to feed livestock or make flour. No investor ordinarily buys stocks to consume either them or their underlying resources. The latter are, of course, legally inaccessible to the shareholders. Instead, stocks are bought for resale, except such few as are from time to time taken off the market in mergers, liquidations, and stock repurchase programs. From year to year, the great majority simply move from hand to hand, bought by shareholders whose expectations of a return of capital and most of the return on capital depend entirely on the willingness of others to share such expectations.[44]

The purchasers of stocks and purchasers of assets have different motivations, and thus, the stock and debt indicator loses much of its credibility as an indicator of the market value of a company's operating properties. Some of the fundamental investment differences between and investment in securities and real or personal property are pointed out by Pratt, Reilly, and Schweihs quoted as follows:

> *Fundamental Investment Difference between Investment Securities and Real Estate/Tangible Personal Property.* Table 29-2 summarizes some of the intrinsic differences between capital market securities (whether debt or equity instruments) and real estate and tangible personal

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[43] Benjamin Graham and David L. Dodd, *Security Analysis*, 2nd ed., (New York: McGraw-Hill, 1940), 10-11.

[44] Louis Lowenstein, *What's Wrong With Wall Street*, 44-45.

property (either individual assets or going concern assemblages of assets) as investment alternatives.

Table 29-2

Investment Differences between Securities and Real Estate/ Personal Property

Securities (Debt or Equity Instruments)	Real Estate/Personal Property (Individually or as a Mass Assemblege)
1. Liquid, marketable investments	1. Illiquid investments
2. Noncontrolling interest in income production and distribution	2. Controlling interest in income production and distribution
3. Small, absolute dollar investment required	3. Large, absolute dollar investment required
4. Small percentage of overall wealth committed to this investment	4. Large percentage of overall wealth committed to this investment
5. Diversified portfolio of investments	5. Nondiversified portfolio of investments
6. Short-term investment time horizon	6. Long-term investment time horizon
7. Does not require re-investment to maintain investment base	7. Requires "replenishment" investment to maintain investment base
8. Investments expected to appreciate over time	8. Investments expected to depreciate over time
9. Income typically subject to only individual tax (from investor's perspective)	9. Income typically subject to both corporate and individual tax (from investor's perspective)
10. Portfolios can be created in limitless combinations of risky securities and risk-free securities	10. Portfolio limited to the particular combination of real estate and personal property that operate the subject business

> As the table indicates, there are fundamental investment risk and return differences between (1) marketable, minority interests in debt and equity securities and (2) nonmarketable, controlling interests in operating real estate and tangible personal property. Due to these differences, and for other reasons, it is unlikely that an economic model that correlates nondiversified risk and expected return for one type of investment will effectively serve the same function for such a different type of investment.[45]

When using the stock and debt approach the liabilities and equity can be summed and the appraiser can deduct the non-operating property to arrive at the indication of market value for the subject property by the stock and debt approach. The computations for the stock and debt approach, including the non-operating property deduction, begin on the following page. These computations are followed by a graphic representation of the stock prices for CSX Corporation for the year 2001 and by the explanation of the stock and debt approach.

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[45] Pratt, Reilly, & Schweihs, *Valuing A Business*, 3rd edition, (Chicago: Irwin Professional Publishing, 1996), 708.

CSX TRANSPORTATION, INC.
Stock and Debt Approach - Stock Allocation Procedure
January 1, 2002

Obligation	Interest Rate	Actually Outstanding	Market Price	Market Value
Equipment Trust Certificates				
CSXT-223	Various	$19,000,000	$106.900	$20,311,000
CSXT-224	Various	20,250,000	103.700	20,999,250
CSXT-225	Various	10,000,000	104.700	10,470,000
CSXT-226	Various	29,400,000	101.600	29,870,400
CSXT-227	Various	18,200,000	109.700	19,965,400
CSXT-228	Various	31,200,000	107.100	33,415,200
CSXT-230	Various	30,400,000	103.000	31,312,000
CSXT-231	Various	34,200,000	103.400	35,362,800
CSXT-232	6.140%	41,203,233	108.500	44,705,507
CSXT-233	Various	42,809,106	100.000	42,809,106
CSXT-234	Various	36,000,000	103.100	37,116,000
CSXT-235	Various	55,000,000	101.200	55,660,000
CSXT-236	Various	60,000,000	97.400	58,440,000
CSXT-237	Various	48,000,000	99.700	47,856,000
CSXT-238	Various	44,400,000	104.600	46,394,000
CSXT-239	Various	66,300,000	107.500	71,272,500
CSXT-240	Various	54,600,000	101.900	55,637,400
Bridged Jets	Libor+	32,054,618	102.400	32,823,824
Total Equipment Trust Certificates		$873,016,857		$894,424,389
Conditional Sales Agreements				
CSXT 422	6.644%	$51,181,000	$101.100	$51,743,991
CSXT 423	6.300%	62,522,236	99.400	62,147,104
CSXT 424	Floating	71,897,000	100.000	71,897,000
CSXT 425	10.250%	1,791,881	100.000	1,791,881
Total Cond. Sales Agreements		$187,392,119		$187,579,976
Capitalized Leases				
CSXT 633	6.180%	$10,013,504	$108.800	$10,894,422
CSXT 634	6.180%	10,713,147	106.800	11,441,841
CSXT 636	7.760%	20,449,827	102.100	20,879,273
CSXT 637	6.830%	12,031,556	102.300	12,308,282
CSXT 638	6.830%	11,599,295	102.300	11,866,080
CSXT 640	8.920%	12,070,790	101.500	12,251,851
CSXT 644	9.570%	6,287,441	107.000	6,727,562
CSXT 646	9.570%	4,545,139	110.000	4,999,653
CSXT 647	9.570%	2,067,228	110.000	2,273,950
CSXT 648	9.570%	3,347,097	107.000	3,581,394
CSXT 656	9.570%	3,877,435	107.000	4,148,856
CSXT 658	9.570%	1,745,082	107.000	1,867,216
CSXT 660	9.570%	1,571,704	107.000	1,681,723
CSXT 662	9.790%	404,811	107.000	433,148
Total Capitalized Leases		$100,724,037		$105,155,050
Mortgage Bonds & Other				
8 LAN 1st Ref Ser 'F'	3.375%	$28,730,000	$95.059	$27,310,451
9 LAN 1st Ref Ser 'G'	2.875%	26,131,000	93.980	24,557,914

CSX TRANSPORTATION, INC.
Stock and Debt Approach - Stock Allocation Procedure (cont.)
January 1, 2002

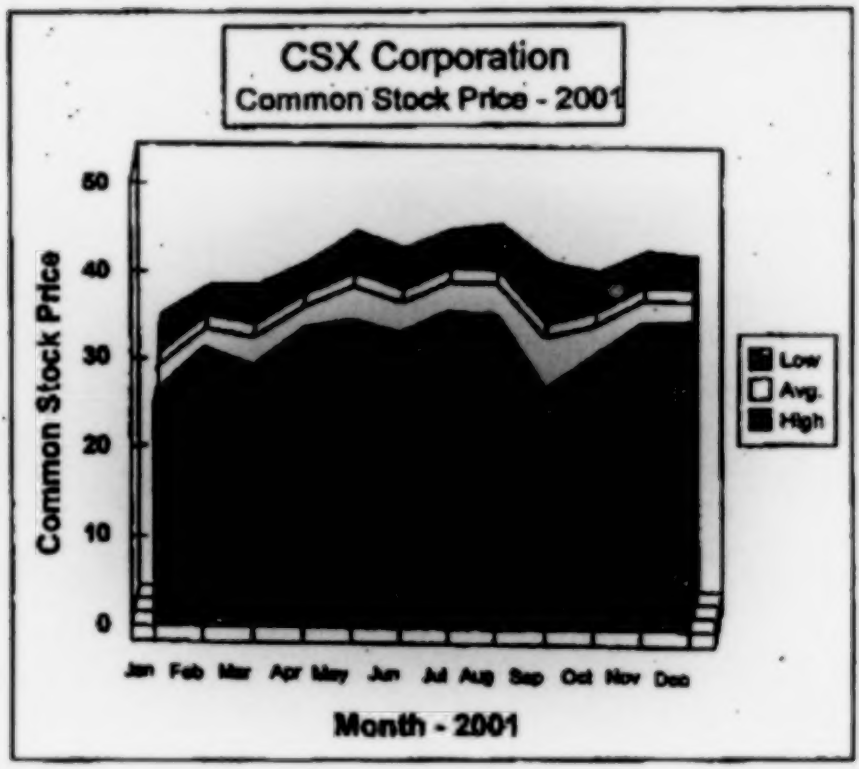
Obligation	Interest Rate	Actually Outstanding	Market Price	Market Value
828 SCL Marion RR Co 6%	6.000%	3,170,000	98.000	3,106,600
536 C&O PPA Rev Bnds 1992	6.000%	17,100,000	102.000	17,442,000
931 for Toledo-Lucas Cty PARB	6.450%	29,700,000	94.000	27,918,000
Total Mortgage Bonds & Other		$104,831,000		$100,334,965
Accounts Payable: Affiliated Companies		$7,188,000	$100.000	$7,188,000
Conrail Long-Term Debt (42%)		485,520,000	100.000	485,520,000
Totals (Long-Term Debt)		$1,588,672,013		$1,580,202,380
Current & Accrued Liabilities		$3,107,577,000	$100.000	$3,107,577,000
Conrail Current & Accrued Liabilities (42%)		167,580,000	100.000	167,580,000
TOTALS (ALL DEBT)		$4,633,829,013		$4,855,359,380
CAPITAL STOCK - COMMON				
CSX Shares Outstanding	Price	CSX Stock Value	CSXT	
213,887,988	$34.59	$7,392,180,075	78.86%	$5,836,866,755
Gross Value of CSXT Stock and Debt				$10,692,068,135
Less: Non-Operating Property			9.87%	1,068,305,941
INDICATION OF VALUE BY STOCK & DEBT APPROACH				$9,636,750,194
			(Rounded)	$9,637,000,000

Computation of Non-operating Property Deduction

Operating Net Plant + Material & Supplies	$16,990,835,227
Total Assets (Operating & Non-Operating)	17,742,738,227
Percent Operating Assets to Total Assets	90.13%
Total Asset Percent	100.00%
Less Operating Asset Percent	90.13%
Non-Operating Asset Percent	9.87%

CSX Corporation
Common Stock Prices During 2001

Month - 2001	High	Low	Average
Jan	$30.54	$24.81	$27.68
Feb	33.99	29.75	31.87
Mar	34.11	27.70	30.91
Apr	36.90	32.05	34.48
May	40.20	33.25	36.73
Jun	38.47	31.60	35.04
Jul	40.72	34.10	37.41
Aug	41.30	33.75	37.53
Sep	36.92	25.44	31.18
Oct	35.98	29.37	32.68
Nov	38.20	32.90	35.55
Dec	37.66	33.45	35.56
Averages	$37.08	$30.68	$33.88
Average Price of CSX Stock For Last 3 Months			$34.59



Explanation of the Stock and Debt Approach

Sales of strictly operating railroad systems such as CSX Transportation Inc. rarely occur. There is a great deal of difficulty in adjusting for dissimilarities in large railroad systems such as operating area, economics of the area served, physical factors, and financial differences. These differences make a comparison virtually impossible even for arms-length sales. For these reasons a sales comparison approach cannot be used in the appraisal of the operating property of CSX Transportation Inc. Partial sales or sales of dissimilar systems will not be indicative of the market value of the operating property of CSX Transportation Inc. We used the stock and debt approach as a substitute for the normal sales comparison approach.

The stock and debt approach (stock allocation procedure) method is based on the accounting principle that assets equal liabilities and equity. In theory, the value of all of the assets on the balance sheet will be the equal to the value of the liabilities on the balance sheet. Because the gross stock and debt value includes all of the liabilities and equity of the business enterprise, it will also include all of the operating and non-operating properties, both tangible and intangible properties. Thus, the non-operating properties must be deducted in order to obtain the market value of the operating assets.

We obtained the market value of the long-term debt of CSX Transportation Inc. from Company officials and checked the reasonableness of these figures with information found in *Mergent Bond Record.* We added the book value of the current liabilities to the market value of long-term debt to obtain a value of all the debt of $4,855,359,380.

For the value of common stock of CSX Transportation Inc. we multiplied the number of shares of common stock of CSX Corporation outstanding at the appraisal date times the aver-

age price of the stock during the last quarter of 2001 to obtain a market value of $7,392,180,075 (213,687,996 shares times $34.59 = $7,392,180,075). This figure was then adjusted by 78.96% to reflect the contribution of the subject company, CSXT, to the parent company, CSX Corp. The calculation is based upon the contribution of CSXT to the total operating income of CSX Corp (or $803,000,000 as a percentage of $1,017,000,000 = 78.96%). Upon summing all of the stock and debt the indicated gross total market value was $10,692,056,135. From this amount we deducted the non-operating property.

To estimate the influence of non-operating properties on the gross stock and debt value, we used the asset ratio method. The asset ratio method compares the operating assets to the total assets to arrive at the operating railroad property percentage of 90.13%. This figure was subtracted from 100.00% to arrive at the non-operating percentage of 9.87%. The non-operating percentage of 9.87% was applied to the gross stock and debt value to arrive at the amount of non-operating property, $1,055,305,941. After deducting the non-operating property from the gross stock and debt value, the indication of value for the operating railroad property of CSX Transportation Inc. by the stock and debt approach as of January 1, 2002, was $9,636,750,194 rounded to $9,637,000,000.

The stock and debt indicator for the appraisal of the operating property of CSX Transportation Inc. should be given much less weight than either the income approach or the cost approach in the final consideration of value. It is certainly clear that one's motives for investing in the stock of a particular enterprise are quite different from the motives of one who purchases the company's operating assets. A purchaser of stock is typically making a relatively short-term investment in a highly liquid instrument of trade. On the other hand, a purchaser of operating assets typically has in mind a

longer term commitment to the use of those assets in order to produce a return thereon.

With differences in motivation by the purchasers of stocks and purchasers of assets, the stock and debt indicator loses much of its credibility as an indicator of the market value of a company's assets. We believe the stock and debt indicator for the operating property of CSX Transportation Inc. serves no useful purpose in the indication of market value. For the indicator of value by the stock and debt approach to have any significant validity, it should be adjusted further for the impact of minority interests being traded and the illiquidity of the assets being appraised versus the prices of stocks being traded. Some studies have suggested that the effect of these two adjustments would be a reduction of the stock prices by approximately 37.5%.[46] Thus, we believe that the stock and debt indicator unadjusted for minority interest and illiquidity discounts must be given very little weight in the overall estimate of value.

Although we considered the sales comparison approach and its surrogate the stock and debt approach, we believe for the reasons stated above that neither a sales comparison approach nor the stock and debt approach is useful in the valuation of the operating assets of CSX Transportation Inc. as of January 1, 2002.

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[46] See Robert F. Reilly, "*Illiquidity Discounts — To Be or Not To Be?,*" paper presented at the Appraisal for Ad Valorem Taxation of Communications, Energy and Transportation Properties Workshop, Wichita State University, August 1997, in which he states that a discount of 37.5% was applied to the capital market values in order to properly estimate the value of the unit of operating property of railroads.

Reconciliation and Value Conclusions

The process of resolving the differences among various value indications is called reconciliation. Reconciliation has been defined by the Appraisal Institute as "*the analysis of alternative conclusions to arrive at a final value estimate.*"[47] It is the bringing of the elements into balance with one another to constitute a unified and coherent whole.

Reconciliation is not just a simple weighing of three approaches; it's the weighing of information used in the various approaches. The process of correlation is continuous from the beginning to the end of the entire appraisal. It is a guiding principle in each major step of the appraisal. All throughout the appraisal process, the appraiser is making decisions, judgments, and evaluating the relevance, importance, and reliability of the data used in each approach.

The indications of value developed by the three approaches to value are as follows:

Value Indicator	Amount
Cost Approach	$6,150,000,000
Income Approach	$5,983,000,000
Stock & Debt Approach	$9,637,000,000

The cost approach was analyzed in detail and given careful consideration. The original cost less depreciation is considered the best starting point in the cost approach. With the deduction of all forms of depreciation, the cost approach can be used to estimate the value of a railroad company, however, as mentioned on page 22, the cost approach offers little insight when valuing the total assets of the business. The cost

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[47] *The Appraisal of Real Estate*, 10th ed., (Chicago: Appraisal Institute, 1992), 553.

approach was given minor consideration in the final opinion of value.

The income approach was also given careful consideration. The potential income stream of CSXT has been analyzed. It was necessary to consider Company projections and other historical and economic data in predicting future income. These estimates were correlated with our own estimates, based on our analysis of the expected earnings. The money market has been analyzed and much study given to the estimation of a reasonable rate of capitalization. A prospective purchaser of railroad property would very carefully consider the earning capability of the property. The income approach is a strong indication of value, and it was given major weight and emphasis in the final opinion of value.

The sales comparison approach could not be used in the ordinary manner as there are no actual arms-length sales of truly comparable properties. The stock and debt approach was considered as a substitute, however there are many problems associated with using traded prices for stocks and securities as surrogates for the value of the underlying assets. The stock and debt as an indicator of value, particularly when the subject company has no traded stock, is rarely useful. Thus for this appraisal we do not believe the stock and debt approach provides any meaningful insight into the market value of the operating assets of CSX Transportation Inc. as of January 1, 2002. For this appraisal report, the stock and debt approach was considered but given no weight in the final opinion of market value.

The basis of this appraisal is the unit method of appraisal. The unit method of estimating the market value for this property is in accordance with generally accepted practice for the appraisal and valuation of properties. It is our belief that a buyer and seller would go through these same processes in an effort to reach a sale price for the operating assets of CSX Transportation Inc. The property is presently serving in the

capacity for which it was constructed. The value conclusion reflects the willing buyer, willing seller concept in an arms-length transaction.

It is not always possible to use three approaches to value in every appraisal. Regarding the reconciliation of the value indicators Dr. Boykin and Dr. Ring state:

> Applying judgment, however, assumes *knowledge* of that to be judged. Thus a reconciliation of the value indicators is not a mathematical or statistical exercise but rather a matter of considered judgment wherein the professional experience and educational training of the appraiser is called upon to determine the final conclusion of value. There might be occasions where only one approach to value is guiding, but generally two or all three approaches contribute in the formulation of the appraiser's judgment. Logic dictates that as a rule the income approach offers the best guide to value since, in the final analysis, value is the "present worth of future rights to income.". . . Since income, however, is the motivating factor for business activities, reason warrants that as a rule the income indicator of value be given the greatest weight, cost lesser weight, and stock and debt the least weight in the final estimate of value.[48]

Thus, reconciliation is not a mathematical exercise but rather a serious judgmental exercise by the professional appraiser to reach a logical conclusion of value.

Final Conclusion of Value

After careful consideration of all pertinent data, and after considering the indications of value, giving the most weight and emphasis to the income approach, less weight to the cost approach, and no weight to the stock and debt approach, it is my opinion that the market value of the system operating

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[48] Alfred A. Ring and James H. Boykin, *The Valuation of Real Estate*, 3rd ed. (Englewood Cliffs, NJ: Prentice-Hall, 1986), 427.

property of CSX Transportation Inc. as of January 1, 2002, was:

SIX BILLION DOLLARS
($6,000,000,000)

Certification

I certify that, to the best of I [sic] knowledge and belief, . . .

- the statements of fact contained in this report are true and correct.
- the reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are my personal, unbiased professional analyses, opinions, and conclusions.
- I have no present or prospective interest in the property that is the subject of this report, and we have no personal interest or bias with respect to the parties involved.
- my compensation is not contingent on an action or event resulting from the analyses, opinions, or conclusions in, or the use of, this report.
- my engagement in this assignment was not contingent upon developing or reporting predetermined results.
- my analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics and the Standards of Professional Practice of the Appraisal Institute and the International Association of Assessing Officers.
- the use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- as of the date of this report, Thomas K. Tegarden has completed the requirements under the continuing education programs of the Appraisal Institute and the International Association of Assessing Officers.
- this appraisal is based on an analysis of financial information and I have not made a personal inspection of the physical property that is the subject of this report.

- no one provided significant professional assistance to the undersigned other than Diane M. Ange, SRA, CAE, who helped gather and record historical financial data.

/s/: Thomas K. Tegarden
THOMAS K. TEGARDEN, MAI, CAE

Assumptions and Limiting Conditions

1. The appraiser did not make a survey of the property. The appraisal of this property is based on an economic approach and none of the property was physically inspected during the course of this appraisal.
2. The appraiser believes that the facts, statements, and opinions contained in this report are reliable and supportable. No responsibility is assumed for the accuracy of information obtained from CSX Transportation Inc., other informed sources, or from other published material which was available.
3. The appraiser assumed that this property is under responsible ownership, is a railroad company, and is under competent management consistent with the regulations.
4. The various approaches to value used in this report may not be considered separately or independently of each other, and the final value conclusion is predicated on a careful reconciliation of all value indicators.
5. The value conclusion in this report represents the appraiser's opinion of the market value of the operating property of CSX Transportation Inc. as of January 1, 2002. The unit method of appraisal has been used in conformance with the recognized appraisal practices for property of this type.
6. The appraiser reserves all rights to the contents and reproductions of this appraisal report, especially conclusions and computations relating to the subject property. No part of this report shall be disseminated to the public through the advertising media, public relations media, news media, or any other public means of communication without the prior written consent of the appraiser.
7. The appraiser may not be required to give testimony or to appear in court by reason to this appraisal, with reference to the property in question, unless prior arrangements have been made therefor.

Professional Qualifications of

Thomas K. Tegarden, MAI, CAE

Tegarden & Associates, Inc., 105 Point East Dr.,
Nashville, TN 37216-1403
(615) 226-2300 Office,
(615)226-4488 FAX

Degrees and Professional Appraisal Designations

B.S. Accounting, Middle Tennessee State University, 1967

MAI (Member, Appraisal Institute) - Appraisal Institute - certified through December 31, 2003 - Member No. 6275

CAE (Certified Assessment Evaluator) - International Association of Assessing Officers - certified through December 31, 2006 - Member No. 516

Tennessee Certified General Appraiser, Tennessee License No. CG-93

Appraisal Education

I have taken numerous appraisal and appraisal related courses conducted by the Appraisal Institute (AI), the International Association of Assessing Officers (IAAO), and other organizations toward the goal of earning the MAI and CAE professional appraisal designations. I received the CAE in 1974 and the MAI in 1981. I have taken several additional appraisal courses through the Appraisal Institute, IAAO, and other organizations in order to maintain a "currently certified" status as an MAI and a CAE to continue to further my appraisal education. I am presently certified as an MAI through December 31, 2003 and as a CAE through December 31, 2006. As of the date of this report I have completed all the requirements under the continuing education program of the AI, the IAAO, and the appraisal license program of the State of Tennessee.

Professional Activities & Memberships

Appraisal Institute

MAI - Member, Appraisal Institute - Certificate #6275
Member of Local Chapter #37
Member of Professional Admissions Committee - Tennessee Chapter #37 – 1982

International Association of Assessing Officers (IAAO)

Member IAAO since 1972
CAE - Certified Assessment Evaluator - Certificate #516
Senior Instructor - IAAO's Educational Program (1983 - present)
Demonstration Report Grader
Chairman - Residential Grading Committee & Chief Review
Grader 1981-90
Member IAAO Course 2 Re-write subcommittee - 1985-86-87
Primary Author IAAO Course 102 - 1993 (*Income Approach to Value*)
One of Three Authors of IAAO Course 101 - 1992-1993
Member IAAO Executive Board - 1982-83
Member Professional Admissions Committee 1980-81
Member Constitutional Review Committee 1979
Professional Designation Advisor - States of KY and TN 1981-85

Faculty Associate - Lincoln Institute of Land Policy Southern Association of State Property Tax Administrators

President -1976, Treasurer - 1975

Tennessee Chapter of IAAO

Published Works

"Future Expectations and Growth: Do They Affect Present Value?," *Journal of Property Tax Management*, Pub. 2:3, Panel Publishers, Inc., (1st Qtr., 1991)

"Inflation and Utility Property Appraisal," *Public Utilities Fortnightly*, Vol. 123, No. 11 (May 25, 1989)

"Controversy in the Valuation of Utility Property: A Rejoinder," *Public Utilities Fortnightly*, Vol. 123, No. 5 (March 2, 1989)

"Appraising Public Utilities: Direct Capitalization and Present Value," *The Appraisal Journal*, January, 1989, The American Institute of Real Estate Appraisers

"Direct Capitalization vs. Yield Capitalization: In the Appraisal of Public Utility Property," *Assessment Digest*, September/October, 1987, International Association of Assessing Officers

"Creative Financing: The Assessor's Viewpoint," *Property Tax Journal*, September, 1983, International Association of Assessing Officers

Awards

1989 recipient of the *Verne W. Pottorff Professional Designee of the Year Award* from the International Association of Assessing Officers. This award is given annually to the IAAO professional designee who has most effectively promoted the interests and goals of the IAAO professional designation program.

1984 recipient of the *Bernard L. Barnard Award* from the International Association of Assessing Officers. This award is given annually to the author of the article published in the *Property Tax Journal* which has contributed the most to the improvement of assessment administration.

Experience

Owner - Tegarden & Associates, Inc. - duties include client consultation, appraisal of public utilities, railroads, special purpose properties, and expert testimony

Was employed by the Tennessee Public Service Commission 15 years — 1967 - 1983 where I was Assistant Director of Assessments for 11 years. My duties included the annual appraisal and assessment of

approximately $4 billion ($4,000,000,000) of railroad and public utility property

Instructor - Seminar on Public Utility Valuation - Wichita State University - sponsored by National Tax Association - Tax Institute of America and Wichita State University

1985 - 2003 "Principles of Appraisal for Public Utility and Railroad Property"

2003 "Advanced Income Approach Issues"

1997 "Advanced Cap Rate Applications"

1993 "DCR Method" and "Weighted After-Tax Cost of Capital and Cap Rate"

1992 "Selection of Income & Rates in Yield Capitalization"

1990 "Future Expectations and Growth: Do They Affect Present Value?"

1986 "Direct Capitalization vs. Yield Capitalization"

1980 "Administrative Problems with Deferred Federal Income Taxes and the Investment Tax Credit"

1978 "Demonstration Appraisal of Telephone Company"

1976 "Special Problems Including Correlation"

Consultant to Georgia Department of Revenue - 1980, 1984,1985, 1998, 1999, & 2000; Missouri State Tax Commission - 1980; Tennessee Attorney Generals Office -1983; Citrus County, FL - 1983; St. Lucie County, FL - 1984; Oklahoma Tax Commission - 1983; Hendry County, FL - 1984; Putnam County, FL - 1990; Dallas County, TX Appraisal District - 1983, 1997; Michigan State Tax Commission - 1985; Florida Department of Revenue - 1985 - 1986; Colorado Legislative Council - 1988-89, Wyoming Tax Commission and State Board of Equalization - 1989 - 1990; Colorado Department of Property Taxation - 1989, 1991, 1993; City of Valdez, Alaska - 1990, 1992; South Dakota Department of Revenue - 1991, 1992; North Slope Borough, Alaska - 1994, 1997; Sarasota County, FL - 1995-96.

Faculty - Land Reform Training Institute (Instructor of appraisal course to students from 12 countries) Taoyuan, Taiwan, Republic of China

Faculty - Lincoln Institute of Land Policy

"The Economic Foundations of Railroad and Utility Valuation," Scottsdale, 1995

"Understanding the Capitalization Process," Scottsdale, AZ, 1994

"The WHYs and HOWs of Railroad and tility Valuation," Scottsdale, AZ, 1991

Senior Instructor - Course 102 - The Income Approach to Valuation (International Association of Assessing Officers) - West Palm Beach, FL; Auburn University; Sarasota, FL; Troy, NY; Jacksonville, FL; Tampa, FL; Columbia, MO; Orlando, FL; Miami, FL; University of Virginia; Denver, CO, Austin, TX, Mississippi State University — 1983 - 2003

Senior Instructor - Contemporary Real Estate Finance (International Association of Assessing Officers) - Montana State University - Bozeman, MT – 1984

Senior Instructor - Introduction to Income Approach to Value Workshop - (International Association of Assessing Officers) Oklahoma City, OK - 1987, Lubbock, TX - 1988

Author and Instructor of copyrighted *Public Utility Basic Appraisal Course*© -LaBelle, FL - 1984; Tallahassee - 1986; Cheyenne - 1989, 1990, 1991, 1992, 1993, 1995, 1996, 1997, 1998, 1999, 2001, 2002, 2003; Austin - 1989; Atlanta - 1992; Denver - 1994; Pierre, SD - 1999

Author and Instructor - *The Development and Use of the Compound Interest Tables* and *Using the HP-12C Calculator* (for Colorado Department of Revenue, 1991 & for International Association of Assessing Officers, 2002)

Program Speaker and Participant - Valuation Roundtable - Phoenix, AZ (Lincoln Institute of Land Policy) - 1984

Program Speaker and Participant - IAAO Public Utility Seminar - New Orleans -2002, Nashville - 1997, New Orleans - 1995

Program Speaker - Annual Professional Seminar - Jointly Sponsored by American Institute of Real Estate Appraisers, International Association of Assessing Officers, and Society of Real Estate Appraisers

17th Seminar - "Creative Financing: The Assessor's View-point" - Kansas City, MO -1982

30th Seminar - "Valuation Issues in the Telecommunications Industry: The Capitalization Rate" - Chicago, IL - 1995

Instructor - CASPER (Computer Assisted Analysis of Special Purpose Properties for Education and Research) - Lincoln Institute of Land Policy - Cambridge, MA - 1982, 1983 - San Francisco, CA -1983, Orlando, FL - 1984

Instructor - Microcomputer Techniques for Special Property Appraisal (Course 109) - Lincoln Institute of Land Policy - Orlando, FL - 1984

Instructor - Institute of Property Taxation - Kellogg School of Business - Michigan State University 1987 "The Appraisal of Railroads and Public Utilities," 1983 "Appraisal of Mineral Interests" and "The Appraisal of Railroads and Public Utilities"

Program Speaker - National Association of Railroad and Public Utility Tax Representatives - Atlanta, GA - 1983; Denver, Colorado - 1986

Instructor - North Carolina IAAO Candidates Club - University of North Carolina - Chapel Hill, NC - 1984

Instructor - International Association of Assessing Officers - Personal Property Seminar - Scottsdale, AZ and Virginia Beach, VA - 1985

Program Speaker - IAAO Conference

Houston, TX - 1996, "Regulation: Its Impact on Value"

Washington, D.C. - 1993, "The Appraisal of Public Utilities & Commercial Properties: What's the Difference?"

Montreal, Quebec - 1990, "The Role of the Consultant in the Ad Valorem Tax Process"

Nashville; TN - 1988, "The Valuation of Public Utilities & the Potential for Growth"

Louisville, KY - 1981, Detroit, MI - 1980, and Atlanta GA - 1976

Expert Testimony

Numerous times - state and federal courts, state assessment boards, public service commissions, and legislative committees as an expert appraisal witness regarding the valuation of public utilities, railroads, special purpose properties, commercial, industrial, and residential properties.

RAILROAD VALUATION WORKSHEET

Tax Year: 2022 Company: CSX Transportation Company No: 176

Summary and Correlation of Unit Value Indicators

Stock & Debt Approach			13,003,785,359
Discounted Cash Flow Analysis			8,139,760,350
Comparable Publicly Traded Company Analysis	Metric Level	Multiple	
	Revenue	2.00	12,348,480,000
	EBITDA	7.60	10,788,011,560
	EBIT	9.50	8,474,791,500
Other			
Book Value (Owned and Leased)			15,809,450,337
UNIT VALUE ESTIMATE			9,290,900,000

Correlation: The discounted cash flow analysis is the preferred methodology for valuing a business and, when adequate data exists, should be given the most consideration.

Analysis of Unit Value Estimate

Percentage of Gross Investment	37.54%
Percentage of Book Value	51.67%
Percentage of Parent Company Gross Stock & Debt	53.66%

Allocation to Georgia

EXEMPT PORTION OF UNIT VALUE	458,000,000	Pollution Control	400,000,000
TAXABLE UNIT VALUE ESTIMATE	7,830,900,000		
System Road Miles	33,397		
Georgia Road Miles	1,679		
Percentage	7.1940239%		
Indicated Georgia Gross Operating Property Value	563,136,693		

Calculation of Georgia Net Taxable Values

	Indicated	Adjusted	Indicated Factor	DOR Factor	DOR Value
Indicated Georgia Gross Operating Property Value	563,136,693	374,080,205			
Deductions: Motor Vehicles	4,156,193	4,156,193			
Pollution Control	3,907,487	7,744,781			
Exempt Line	38,210,371	28,170,053			
Total Taxable FMV of operating property in GA	514,862,671	337,023,203	1.52758176	1.52758176	514,862,672
Total Taxable FMV of non-operating property in GA	27,907,489	27,758,511			27,907,489

Deduction Calculations

Pollution Control			PMLA		
Gross Investment	7,744,781		% of Georgia Total	18.91285%	
FMV %	37.54%		PMLA FMV	84,342,316	
FMV	3,907,487		Op. Real Estate	5,773,379	
			Track & Rolling Stock	75,518,941	
			Track (50%)	38,259,471	
			Side Track	49,000	
			Exempt Main Line	38,210,371	

Historical Information

End of Year TAX Data

Operating Company				Parent Company		
Income Statement				Balance Sheet		
Mat. & Supplies	181,369,000			Mat. & Supplies	306,000,000	
Income Statement				Current Assets	2,574,000,000	
Misc. Rent Income	13,600,000			Total Assets	29,871,000,000	
Income from Lease of R&E	4,765,000			LTD (Incl. Maturities)	1,944,000,000	
Rent for Leased R&E	123,588,000			Current Liabilities	3,365,000,000	
Leased R&E Depr. (net)	79,948,000			Long Term Debt	8,839,000,000	
R-1 Sch 352a				Income Statement		
Investment in Prop	19,234,000,000			Revenues	8,119,000,000	
Oper. & Accum.	5,537,000,000			Expenses	7,883,000,000	
Leased Equipment Sch.				Other Income	9,000,000	
Original Cost	3,609,040,571			Cash Flow Statement		
Depreciated Cost	1,702,041,227			Depreciation	923,000,000	

	1996	1997	1998	1999	2000	2001
Historic Income Data						
Operating Revenue	-	-	4,956,000,000	5,423,000,000	6,075,000,000	6,383,000,000
Operating Expense	-	-	3,953,000,000	4,294,000,000	5,468,000,000	5,394,000,000
Depreciation & Amortization	-	-	450,000,000	488,000,000	630,000,000	550,000,000
Operating Ratio	0.00%	0.00%	79.80%	83.33%	90.00%	87.59%
Capital Expenditures	-	-	1,213,000,000	1,298,000,000	923,000,000	848,000,000
Historic Rate of Change						
Operating Revenue				13.48%	8.64%	8.13%
Operating Expense				21.31%	15.80%	-3.69%
Depreciation & Amortization				8.00%	7.00%	9.77%
Operating Ratio				6.92%	5.43%	3.20%
Capital Expenditures				7.10%	-36.67%	3.16%

PLAINTIFF'S EXHIBIT 32

Discounted Cash Flow Analysis

The discounted cash flow analysis most clearly replicates the actions of the market in valuing a company or investment. It is founded on the principle that the value of any investment is equal to the present worth of all future cash benefits to be derived from ownership of the investment. The model used calculates the future operating free cash flows for ten years and a reversion value at the end of that period based on a limited number of assumptions relative to revenue, expense, and capital expenditure patterns. When insufficient data exists upon which to base these assumptions, the model is extremely useful for testing the reasonableness of the result of other approaches to value.

Predicted Variables for Discounted Cash Flow Analysis

Operating Revenue Rate of Change	1.50%
DA Rate of Change	3.00%
Capital Expenditure Rate of Change	4.00%
Target Operating Ratio	80.00%
Income Tax Rate	39.00%

Discounted Cash Flow Analysis

Year	2002	2003	2004	2005	2006	2007
Operating Revenue	8,173,230,000	8,265,628,450	8,348,815,877	8,435,313,115	8,522,041,312	8,650,321,932
Operating Expense	6,333,670,720	6,388,914,042	6,440,843,493	6,498,269,643	6,470,984,456	6,506,486,540
Net Rent for Road	118,791,000	118,791,000	118,791,000	118,791,000	118,791,000	118,791,000
Misc. Rent Income	13,560,000	13,560,000	13,560,000	13,560,000	13,560,000	13,560,000
EBITDA	1,836,430,280	1,911,679,408	1,987,343,332	1,771,324,518	1,931,056,857	1,952,985,135
Depr. & Amort.	586,000,000	663,495,000	600,000,834	619,229,848	627,833,741	654,778,783
Depr. On Leased Road	79,848,000	79,848,000	79,848,000	79,848,000	79,848,000	79,848,000
EBIT	692,082,280	848,336,408	1,006,495,342	1,072,446,672	1,133,809,916	1,198,378,372
IT (39%)	347,912,988	368,939,223	392,533,199	418,254,202	442,187,829	466,947,583
Net Income	644,170,191	579,807,245	615,962,183	654,192,470	691,501,988	728,790,807
Operating Ratio	88.40%	85.70%	85.00%	84.20%	83.50%	82.60%
Change in Working Cap	1,784,227	1,885,772	1,943,838	651,324	1,424,513	1,385,337
Capital Expenditures	681,920,000	917,196,800	953,884,672	992,040,059	1,031,731,661	1,072,996,927
Operating Free Cash Flow	306,933,964	323,187,673	339,381,722	360,979,921	379,904,555	382,011,709
% change		5.32%	5.07%	6.10%	4.37%	0.21%
Reversion						
Total Cash Flow	306,933,964	323,187,673	339,381,722	360,979,921	379,904,555	382,011,709

Year	2008	2009	2010	2011	Market Multiple	Proceeds
Operating Revenue	8,758,978,761	8,831,327,912	8,954,997,451	7,269,409,294	2.00	14,118,818,588
Operating Expense	6,541,813,921	6,579,880,820	6,611,958,992	5,848,737,458		
Net Rent for Road	118,791,000	118,791,000	118,791,000	118,791,000		
Misc. Rent Income	13,560,000	13,560,000	13,560,000	13,560,000		
EBITDA	2,017,083,364	2,165,441,537	2,195,137,133	2,282,205,909	7.00	15,982,440,363
Depr. & Amort.	674,430,836	696,723,648	717,825,251	739,154,909		
Depr. On Leased Road	79,848,000	79,848,000	79,848,000	79,848,000		
EBIT	1,268,786,740	1,329,469,902	1,394,863,881	1,464,204,980	9.50	13,909,948,170
IT (39%)	491,706,829	517,479,257	543,818,914	571,039,943		
Net Income	768,079,911	808,380,685	850,744,967	893,164,963		(Discounted value of all future cash flows growing at a rate of 8.7%)
Operating Ratio	82.10%	81.40%	80.70%	80.00%		
Change in Working Cap	1,939,717	1,259,582	1,172,860	1,103,478		
Capital Expenditures	1,115,912,148	1,160,548,554	1,206,968,418	1,255,247,153		
Operating Free Cash Flow	408,144,672	434,178,104	440,978,942	455,918,343		13,459,243,084
% change	6.82%	3.83%	2.75%	3.58%		
Reversion				13,459,243,084		
Total Cash Flow	408,144,672	434,178,104	440,978,942	13,915,080,027		

	WACC	min	point est.	max
		9.30%	9.80%	10.20%
Indicated Value		7,877,732,465	7,518,317,143	7,249,123,651
Indicated Lsd. Eq. Adj.		622,190,081	607,978,209	601,873,881
Indicated Adj. Value		8,499,922,824	8,126,293,348	7,847,196,592

Leased Property Expense Adjustments

The operating cost of the public utility or railroad being valued is to include all operating assets owned or used in the utility or railroad operation. Therefore, the value of the utility or railroad company should be based on the income it would produce if it owned all operating assets. While the revenues produced by leased assets are already included in the operating revenues, the expenses are not properly recognized for. If the leased assets were owned by the operating company, the company would not have the lease payments associated with those assets but would be allowed the appropriate depreciation expense.

Annual Rent	2002	2003	2004	2005	2006	2007
Per Schedule	245,508,230					
Deductions	46,654,000	79,033,501	1,340,569	(60,439,457)	83,749	180,838
Adjustment	248,881,230	168,817,883	168,427,302	117,867,845	117,884,096	117,725,354

		2008	2009	2010	2011
	Deductions	2,915,748	5,910,410	3,119,290	-
	Adjustment	114,809,780	108,899,370	103,783,080	103,783,080

Annual Depreciation	2002	2003	2004	2005	2006	2007
Per Schedule	128,144,757					
Deductions	34,378,143	34,743,654	393,831	37,173,161	16,834	168,139
Adjustment	93,766,615	88,024,991	88,831,330	31,469,169	31,442,535	31,276,469

		2008	2009	2010	2011
	Deductions	1,088,393	2,451,365	2,487,736	-
	Adjustment	30,217,617	27,765,452	25,277,672	25,277,672

Leased Equipment Adjst	0	0	0	0	0	0
EBITDA	248,881,230	168,817,883	168,427,302	117,867,845	117,884,096	117,725,354
DA	93,766,615	88,024,991	88,831,330	31,469,169	31,442,535	31,276,469
EBIT	155,087,615	100,792,892	99,795,972	86,398,676	86,451,561	86,448,885
IT (39%)	60,483,330	39,309,147	38,920,429	33,748,184	33,716,109	33,715,164
op inf	188,309,010	130,508,816	129,506,873	84,249,661	84,177,987	84,010,190

		0	0	0	0
	EBITDA	114,809,750	168,899,350	103,783,080	103,783,080
	DA	30,217,617	27,765,452	25,277,672	25,277,672
	EBIT	84,592,743	81,133,898	78,505,388	78,505,388
	IT (39%)	32,991,170	31,642,332	30,617,101	30,617,101
	op inf	81,818,590	77,257,118	73,166,988	73,166,988

Stock & Debt Approach

The value of a company whose equity and debt securities are traded in the marketplace is determined by the sum of the values of those securities plus the net of its current liabilities less current assets. Unfortunately, the public utility and railroad companies being valued by the Department of Revenue are rarely publicly traded, but are often subsidiaries of such companies. Even when they are traded, not all of their assets are operating. At best, an educated guess of the portion of the total traded company's value attributable to the operating assets can be made. The more pure the traded company is, the more reliable the estimate can be deemed. This method is not applicable to valuing the operating assets of a public utility or railroad that is neither publicly traded nor has a publicly traded parent company.

TRADED PARENT COMPANY : CSX Corporation

January 1, 2002

			# of Shares	Price/Share	Market Value
		Stock	213,647,996	35.09	7,598,745,136
		LTD		Book Value	
				6,960,000,000	7,200,000,000
		Current Liabilities - Current Assets			381,000,000
		Gross Stock & Debt Value			15,219,745,136
		Operating Allocation			
	Revenues	EBITDA	EBIT	Assets	
Operating	8,982,004,000	1,349,540,000	709,680,000	14,286,794,000	
Total Company	8,115,000,000	1,648,000,000	1,026,000,000	18,933,000,000	
Percentage	74.07%	81.88%	77.83%	75.47%	75.09%
		Indicated System Operating Property Value			11,414,809,000
		Plus Leased Equipment			867,979,399
		Adjusted Indicated System Operating Property Value			12,282,784,399
		Notes:			
		Current Assets(-Asset)		1,884,000,000	
		Current Liabilities(-Curr.Liab)		2,265,000,000	

Comparable Publicly Traded Company Analysis

Income Level	Multiple	$	Financial Ratios	
Revenues	2.50	13,345,458,999	Payout Ratio	88.29%
EBITDA	7.00	10,793,911,943	Sales to Total Assets	38.85%
EBIT	9.50	9,474,791,944	Current Ratio	62.79%
			Operating Margin	24.82%

RAILROAD COST OF CAPITAL AND MARKET MULTIPLE STUDY

COST OF CAPITAL

The cost of capital is estimated by a band of investment method that combines estimated costs of equity and debt utilizing a market capital structure typical for the industry. An after tax cost of debt is utilized; therefore the estimated WACC (weighted average cost of capital) should be used to discount unleveraged after tax free cash flows.

COST OF EQUITY

The cost of equity is estimated based on a discounted cash flow model (DCF) and the capital asset pricing model (CAPM). The DCF derives the discount rate that equates the present value of future benefits (dividends and reversion) with the current price. In this application, d1 is the ValueLine estimate, P is a normalized year-end price based on an average of the fourth quarter monthly highs and lows, a trended year's monthly highs and lows, and the year end price, and g1 and g2 are short (3 year) and long term (years 4 through 10) growth rates based on ValueLine's projected earnings and assumption of the growth rate for the Gross National Product respectively. The reversion is based on the assumption that the price will change at the same rate as the dividend. The (CAPM) is based on the formula Ra = Rf + B x Rp where Rf is the risk free rate, B is the beta for the company's stock, and Rp is the risk premium. In this application, Rf and Rp are the long term variables published by Ibbotson Associates and the beta is the number published by ValueLine.

STOCK DATA — 2001 — 2002 — 2002 — 2005

COMPANY	CHOSEN YR END PRICE (P)	ESTIMATED DIVIDEND (d_1)	ESTIMATED EARNINGS	ESTIMATED EARNINGS	ESTIMATED 3 YEAR EARNINGS GROWTH (g1)	BETA
BURLINGTON NORTHERN SANTA FE RR	27.48	0.48	2.25	3.20	12.6%	0.95
CANADIAN NATIONAL RAILWAY	48.67	0.60	3.40	4.30	8.1%	0.86
CANADIAN PACIFIC RAILWAY LTD	18.67	0.33	1.80	2.25	12.0%	
CSX CORP	35.28	0.40	2.30	3.80	16.1%	1.10
NORFOLK SOUTHERN CORP	18.32	0.24	1.05	1.65	16.3%	1.05
UNION PACIFIC CORP	54.15	0.80	4.20	6.85	11.7%	0.90
Real GDP + GDP Price Index (VL) (gZ)	6.3%					
Long-Term Riskless Rate (20 year)	5.8%					
Equity Risk Premia (long-horizon)	7.4%					

INDICATORS

COMPANY	UNLEVERED BETA	DCF	CAPM	CAPM TYP CAP STRUCT	SIZE CAP	EQUITY %
BURLINGTON NORTHERN SANTA FE RR	0.89	9.4%	12.63%	12.98%	LARGE	61.4%
CANADIAN NATIONAL RAILWAY	0.77	7.8%	12.63%	13.62%	LARGE	72.8%
[redacted]						
CSX CORP	0.71	8.8%	13.84%	13.19%	LARGE	52.1%
NORFOLK SOUTHERN CORP	0.83	10.0%	13.57%	12.36%	LARGE	47.9%
UNION PACIFIC CORP	0.85	8.8%	12.46%	12.57%	LARGE	61.5%
MEDIAN OF ALL COMPANIES	0.89	9.00%	13.00%	13.00%		
MEDIAN OF LARGE CAP COMPANIES	0.89	9.36%	12.63%	12.98%		

CONCLUSIONS

Based on the indicators, it is my opinion that the cost of equity for large cap railroad companies with a typical capital structure is as follows:

	Minimum	Maximum	Point Estimate
Large Cap Companies (over $5,252 million)	12.0%	13.5%	13.0%

Based on this opinion and the size premia published by Ibbotson Associates, it is my opinion that the cost of equity for smaller railroad companies is as follows:

	Size Premia	Minimum	Maximum	Point Estimate
Mid Cap Companies ($1,115 to $5,252 million)	0.7%	12.7%	14.2%	13.7%
Low Cap Companies ($269 to $1,115 million)	1.4%	13.4%	14.9%	14.4%
Micro Cap Companies (below $269 million)	3.3%	15.3%	16.8%	16.3%

CAPITAL STRUCTURE

The typical market capital structure is estimated by comparing a company's market value of equity and market value of debt with its total market value of equity and debt. The market value of equity is estimated by multiplying the price per share times the number of shares. The market value of debt is estimated with the book value of debt. For use in calculating market multiples, a company's total market cap is the value of equity plus the value of debt less cash. Numbers published in ValueLine are used for number of shares, total debt and cash.

COMPANY	CHOSEN YR END PRICE	NUMBER OF SHARES	VALUE OF EQUITY (MILLION)	TOTAL DEBT (MILLION)	CASH (MILLION)	TOTAL MARKET CAP (MILLION)
BURLINGTON NORTHERN SANTA FE RR	27.48	365,874,903	10,026	6,684	20	17,290
CANADIAN NATIONAL RAILWAY	45.87	182,000,000	8,507	3,274	531	11,550
CANADIAN PACIFIC RAILWAY LTD	16.67	156,184,200	2,953	2,362	68	5,247
CSX CORP	35.29	213,162,313	7,520	6,907	592	13,835
NORFOLK SOUTHERN CORP	18.32	385,528,270	7,063	7,668	134	14,597
UNION PACIFIC CORP	54.15	248,406,619	13,451	8,404	120	21,735
AGGREGATE			60,420	35,299		
BURLINGTON NORTHERN SANTA FE RR			61.4%	38.6%		
CANADIAN NATIONAL RAILWAY			72.9%	27.1%		
CANADIAN PACIFIC RAILWAY LTD			55.6%	44.4%		
CSX CORP			52.1%	47.9%		
NORFOLK SOUTHERN CORP			47.9%	52.1%		
UNION PACIFIC CORP			61.5%	38.5%		
AGGREGATE			58.8%	41.2%		
TYPICAL		SAY	60.0%	40.0%		

COST OF DEBT

The cost of debt is estimated based on the S&P long term ratings for companies in this business sector, being mindful of the individual company's capital structures and the typical capital structure selected.

COMPANY	S&P LONG TERM RATING	S&P CORPORATE BOND YIELD	NOMINAL INCOME TAX RATE	AFTER TAX COST OF DEBT
BURLINGTON NORTHERN SANTA FE RR	BBB+			
CANADIAN NATIONAL RAILWAY				
CANADIAN PACIFIC RAILWAY LTD	A-			
CSX CORP	BBB			
NORFOLK SOUTHERN CORP	BBB			
UNION PACIFIC CORP	BBB-			
SELECTED AS TYPICAL	BBB	6.47%	39.0%	6.17%

WEIGHTED AVERAGE COST OF CAPITAL (AFTER TAX)	Minimum	Maximum	Point Estimate
Large Cap Companies (over $5,252 million)	9.3%	10.2%	9.9%
Mid Cap Companies ($1,116 to $5,252 million)	9.7%	10.8%	10.3%
Low Cap Companies ($269 to $1,116 million)	10.1%	11.0%	10.7%
Micro Cap Companies (below $269 million)	11.2%	12.1%	11.8%

MARKET MULTIPLES

Market multiples are calculated by comparing each company's total market capitalization to various levels of income. In this application, market multiples are developed for revenues, for earnings before interest, taxes,depreciation and amortization (EBITDA), and for earnings before interest and taxes (EBIT). Various financial ratios are also developed for each company for use in evaluating comparability to the company being valued. The amounts of income are these estimated for the next year.

INCOME DATA

COMPANY	TOTAL MARKET CAP (MILLION)	REVENUES (MILLION)	OPERATING MARGIN	EBITDA (MILLION)	DEPRE- CIATION	EBIT (MILLION)
BURLINGTON NORTHERN SANTA FE RR	17,289	9,280.0	31.0%	2,876.8	940.0	1,936.8
CANADIAN NATIONAL RAILWAY	11,550	3,550.0	43.5%	1,544.3	355.0	1,189.3
CANADIAN PACIFIC RAILWAY LTD	5,247	2,440.0	33.5%	817.4	230.0	587.4
CSX CORP	13,835	8,320.0	22.5%	1,872.0	640.0	1,232.0
NORFOLK SOUTHERN CORP	14,587	8,155.0	26.0%	1,600.3	520.0	1,080.3
UNION PACIFIC CORP	21,735	12,200.0	28.5%	3,494.1	1,200.0	2,294.1

MULTIPLES

COMPANY	REVENUES	EBITDA	EBIT
BURLINGTON NORTHERN SANTA FE RR	1.86	6.01	8.93
CANADIAN NATIONAL RAILWAY	3.25	7.48	9.71
CANADIAN PACIFIC RAILWAY LTD	2.15	6.42	8.93
CSX CORP	1.66	7.39	11.23
NORFOLK SOUTHERN CORP	2.37	9.12	13.51
UNION PACIFIC CORP	1.77	6.22	9.47
MEAN	2.18	7.11	10.30
MEDIAN	2.01	6.91	9.59

Many financial ratios can be developed from data already presented in this study. Additional data is presented below, followed by the computed ratios for each company. Following the financial ratios are definitions of each of the ratios. Other ratios with their definitions are then presented. All the ratios are considered as measurements of comparability to other companies.

ADDITIONAL DATA

COMPANY	TOTAL ASSETS (MILLION)	CURRENT ASSETS (MILLION)	CURRENT LIABILITIES (MILLION)
BURLINGTON NORTHERN SANTA FE RR	24,741	965	2,266
CANADIAN NATIONAL RAILWAY	18,801	2,009	1,638
CANADIAN PACIFIC RAILWAY LTD		743	762
CSX CORP	20,808	2,019	3,447
NORFOLK SOUTHERN CORP	19,385	893	2,383
UNION PACIFIC CORP	31,305	1,309	2,824

FINANCIAL RATIOS

COMPANY	PAYOUT RATIO	SALES TO TOTAL ASSETS	CURRENT RATIO	OPERATING MARGIN
BURLINGTON NORTHERN SANTA FE RR	21.3%	37.5%	43.8%	31.0%
CANADIAN NATIONAL RAILWAY	17.8%	18.9%	130.9%	43.5%
CANADIAN PACIFIC RAILWAY LTD	20.6%		98.8%	33.5%
CSX CORP	17.4%	40.4%	58.6%	22.5%
NORFOLK SOUTHERN CORP	22.9%	31.8%	37.8%	26.0%
UNION PACIFIC CORP	19.0%	39.2%	49.5%	28.5%

DEFINITIONS

PAYOUT RATIO	Next year's estimated dividend divided by next year's estimated earnings
SALES TO TOTAL ASSETS	Next year's estimated revenues divided by total assets from most recently available balance sheets
CURRENT RATIO	Current assets divided by current liabilities from most recently available balance sheets
OPERATING MARGIN	Next year's estimated EBITDA divided by next year's estimated revenues

OTHER RATIOS

COMPANY	ESTIMATED 3 YEAR COMPANY GROWTH
BURLINGTON NORTHERN SANTA FE RR	7.6%
CANADIAN NATIONAL RAILWAY	5.8%
CANADIAN PACIFIC RAILWAY LTD	-0.7%
CSX CORP	8.4%
NORFOLK SOUTHERN CORP	7.8%
UNION PACIFIC CORP	7.2%

DEFINITIONS

EST. 3 YEAR COMPANY GROWTH	Estimated 3 year earnings growth times the equity percentage of equity plus total debt.

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REVISED APPRAISAL

OF

THE FAIR MARKET VALUE

OF

ALL PROPERTY OWNED, OPERATED, OR USED BY

CSX TRANSPORTATION, INC.

IN PROVIDING RAILROAD TRANSPORTATION SERVICES

AND

ALLOCATION OF THE FAIR MARKET VALUE

TO THE TAXABLE OPERATING ASSETS IN GEORGIA

GREGG DICKERSON
PROGRAM MANAGER
GEORGIA DEPARTMENT OF REVENUE
PROPERTY TAX DIVISION

[Defendant's Ex. 14]

* * * *

Addendum E

A. Qualifications

I received my B.S.Ed degree from the University of Georgia in 1972. Since that time I have taken numerous courses and examinations involving the theories and methodologies of property valuation, have spoken and published on those topics, and have actively worked as a property appraiser. I am currently employed as Program Manager, Public Utilities Section, Property Tax Division, in which capacity I am responsible for determining fair market values for ad valorem tax purposes of operating property in Georgia owned by public utilities (including railroads) and certain other taxpayers.

In 1973 I successfully completed a training course in all aspects of real estate appraisal conducted by O. R. Colan and Associates, Orlando, Florida and sponsored by the Georgia Department of Transportation. I subsequently took and passed the American Institute of Real Estate Appraisers examinations for Basic Appraisal Theory (Course 1A), Introduction to the Income Approach (Course 1B), and Advanced Income Approach (Course 2).

For 18 of the past 19 years I have attended the Appraisal for Ad Valorem Taxation of Communications, Energy and Transportation Properties program sponsored by the National Tax Association and Wichita State University, which is the largest national educational program dealing with the theory of and current issues in the valuation of public utilities and railroads for property tax purposes. It is attended by several hundred people involved in this discipline from industry, academia, the consulting profession, and state and local governments. Speakers from these and other related fields present papers or participate in discussions on all topics related to the property taxation of public utilities, airlines, and

railroads. I have also been a frequent speaker at this program on such topics as the income approach, the use of market multiples and the stock and debt approach as they apply to unit rule valuation of public utilities and railroads, and I have been a member of the planning committee that annually reviews the questionnaires submitted by attendees of the program to decide on the topics and speakers for the next program, as well as the structure of the program.

I have been a frequent speaker at the International Association of Assessing Officers' Public Utility Seminars, which are devoted entirely to issues involving the valuation of property owned by railroads and public utilities, and annual conferences.

I have taught unit rule valuation methodologies at both state and national educational programs, including a 40 hour introductory course on the valuation of public utilities for property taxes at the Georgia Department of Revenue's Annual Short Course for county appraisers and a portion of the basic course taught at the Appraisal for Ad Valorem Taxation of Communications, Energy and Transportation Properties program sponsored by the National Tax Association and Wichita State University.

Articles that I have written on such topics as discounting of owner financing and application of the income approach in unit rule appraisals have been published in "The Appraisal Journal," "Assessment Digest", and "The Property Tax Journal," which are national publications in the property appraisal and property assessment fields.

I am certified as an Appraiser IV by the Georgia Department of Revenue's Georgia Certification Program.

From 1973 to 1983 I was employed by the Georgia Department of Transportation as a Right of Way Appraiser I, II, and Team Leader. In that capacity I prepared and reviewed appraisals of varied types of real estate for purposes of right-

of-way acquisition. I was employed by the Georgia Department of Revenue as Public Utility Valuation Manager from 1983 to 1993. In this position I prepared unit rule appraisals of all types of public utilities and railroads for Georgia ad valorem tax purposes. I was hired by Norfolk Southern Corporation in 1993 as a Property Tax Manager, where I was responsible for reviewing appraisals of the properties of Norfolk Southern's railroad subsidiaries made by the states in which those companies had property and negotiating unit valuations with them. In 2001 I returned to the Georgia Department of Revenue to assume my present position.

B. Prior Publications

The publications that I have authored within the preceding ten years consist of the following papers.

Published in the proceedings of the annual program on "Appraisal for Ad Valorem Taxation of Communications, Energy and Transportation Properties" sponsored by the National Tax Association and Wichita State University:

(1) "The Great Operating Lease Debate, or You Knit, Therefore You Are" (2000);
(2) "Estimating the Cost of Equity, or They Ripped Out My CAPM and Stomped That Sucker Flat" (1997)
(3) "Income to be Capitalized for Direct Capitalization, or Which Came First, the Chicken or the Egg?" (1992)
(4) "Metaphysics and NOI Growth: A Leap of Faith" (1991)
(5) "Unconglomerating the Conglomerate, or Dissecting a Frog with a Chainsaw" (1989).

I have submitted an article entitled "Advanced Cost of Capital Issues" for publication in the proceedings of the upcoming 2004 Wichita program.

Published in the International Association of Assessing Officers (IAAO) Annual Conference Proceedings:

(1) "Estimating The Cost Of Equity" (1997); and

(2) "Exploring Capitalization: Will The Direct Avenue Yield Sound Unit Values" (1995).

C. Prior Testimony

I have testified as an expert by deposition within the preceding four years in the following cases:

(1) *Florida Power & Light Co. v. Bart L. Graham, et al.*; Fulton Superior Court; Civil Action No. 2003CV77899. Deposed on the value of Florida Power & Light as of January 1, 2003.

(2) *CSX Transportation, Inc. v. The State Bd. of Equalization, et al.*; U.S. Dist. Ct (N.D. Ga.); Civil Action No. 1:02-CV-2634CAP. Deposed on the value of CSX Transportation as of January 1, 2002.

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

No.1:02-CV-2634

CSX RAILROAD TRANSPORTATION, INC.
Plaintiff,

vs.

STATE BOARD OF EQUALIZATION,
Defendant.

TRIAL TRANSCRIPT

VOLUME II - MAY 17, 2005

BEFORE THE HON. CHARLES A. PANNELL, JR.

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VOLUME II

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WITNESS	DIRECT	CROSS	REDIRECT	RECROSS
Gregg Dickerson	203	292	322	
Carl Martland	327	346	363	

* * * *

[206] Q. Now, just so I'll be clear, when you worked — Well, let me start off to be sure we are correct. The appraisals you are doing now or the work you are doing now at the Department of Revenue, for the most part, and certainly the appraisal you are doing in this case, is under the unit value methodology, correct?

A. In value, yes. In numbers of companies, it's probably the other way around.

Q. Sure. You do 200 private car lines, and you don't do those as unit values?

A. That's correct, and there are 300 of them.

Q. Okay. I knew there was a lot of them. But the big guys, the Georgia Powers, the BellSouths, the Atlanta Gas, that's the bulk of your digest, and you do those as a unit valuation?

A. That's correct.

Q. Okay. When you were at the Department of Transportation for those ten years, you didn't do any unit valuations?

A. No, sir.

Q. Okay. And I think you told me earlier that when you were at Norfolk Southern, you didn't do any unit appraisals?

A. That's correct.

Q. Okay. Now, you do not hold an appraisal designation from the Appraisal Institute, is that correct?

A. No, sir.

Q. And I think you have told me before that the only [207] appraisal course you have taken, formal course was one on real estate appraisal you took back in 1973?

A. That's correct.

Q. Okay. And did you also tell me that the appraisal that you have done in this case, the written appraisal, which was defendant's number 77, that's really the first formal written appraisal that you have ever done?

A. First formal written unit rule appraisal.

Q. Yes, sir. All right. So just to be clear, you have taken one formal appraisal course about thirty-two years ago in 1973, correct?

A. Correct.

Q. And that didn't involve unit appraisal at all?

A. That's correct.

Q. And the appraisal you are going to be presenting here is the first formal unit appraisal you have ever presented?

A. The first full written appraisal, yes, or narrative appraisal.

Q. Okay. Now, Mr. Dickerson, I want to talk about your valuation work sheet, that's plaintiff's exhibit number 32. Do you have a copy of that with you?

A. No, sir.

Q. Okay. Let's see if we can get you one. I'll give you this one and move this thing along. That's the work sheet that forms the basis of the proposed assessment in this case, is

* * * *

[257] correct problems that he saw with CSX.

THE COURT: Well, I agree with you that it may not be — it may not be determinative. It may be probative. So I'll overrule your objection.

MR. MCBRIDE: I believe I'm going to tie this together, Your Honor. I'll do my best.

THE COURT: I hope I'm there when you tie it all together, mentally.

MR. MCBRIDE: I'll do it as fast as I can.

THE COURT: All right. Go ahead.

Q. Okay. Now, just to make the point, if I look down to the other large company there, that's Norfolk Southern Railway Company, correct?

A. Norfolk Southern Combined Railway, yes, sir.

Q. Okay. And you increased their value between 2001 and 2002 by 19.88?

A. That's correct.

Q. And, again, looking across the page, I can show what's happened with respect to their Georgia taxable value, correct?

A. Yes, sir.

Q. Okay. Now, I believe you and I talked at deposition, and I don't want to have to go through all of these pages. But of the large taxpayers that you have in Georgia, the BellSouths, the Georgia Powers, nobody got an increase anything like the 47 percent or the 19 percent that the railroads got, right?

[258] MR. CALVERT: Just for the record, Your Honor, we renew the same objection.

THE COURT: Right, it is noted.

A. I believe that's true.

Q. We talked about that on deposition. Okay. And that's because you knew a lot about these railroads, and you knew how to go and try to determine what you really thought the value of these railroads was, right? You knew a lot about evaluating railroads, and you felt comfortable increasing these railroads by very significant percentages, didn't you?

MR. CALVERT: Your Honor, Mr. McBride is leading. He's got compound questions there. We would object to that.

THE COURT: Well, he is an expert witness. I think he can handle that.

MR. MCBRIDE: And, Your Honor, under 611, I'm entitled to lead this witness. He's the guy who did the appraisal against us.

THE COURT: I'm going to let ask you that question. Go ahead.

MR. MCBRIDE: Pardon me?

THE COURT: You are going to get to ask that one.

MR. MCBRIDE: Okay.

THE WITNESS: Could you repeat the question?

(Record was read as requested)

Q. You want me to break that down into some more questions,

* * * *

[297] MR. CALVERT: In that case, I didn't want to waive any objections by questioning from this document, but I'll proceed.

Q. Mr. Dickerson, on this particular document, the number I'm pointing to, the 9.7 billion dollar number for CSX?
A. Yes, sir.
Q. What does that represent?
A. That would have been my lower limit of value, of unit value for the year 2003.
Q. Okay. Now, what was your lower limit of value for 2002, for unit value?
A. The one that was in the valuation work sheets was 8.2 billion.
Q. And that's the number that was—the proposed assessment for 2002 was based on?
A. Yes, sir.
Q. Now, for 2003, was the proposed assessment against — issued against CSXT based on a unit value of 9.7?
A. Yes, sir.
Q. Okay. Now, following across on the same document, under the column marked CY unit value, and that reflects current year unit value, correct?
A. Correct.
Q. That shows 10.767 billion dollars. You see that number?
A. Yes, sir.
Q. And what does that number represent?

[298] A. That is my estimate of the lower limit of unit value for CSX Transportation for the year 2004.

Q. See the number under the column marked CY Georgia FMD?

A. Yes, sir.

Q. What does that number represent?

A. That represents the taxable Georgia fair market value for CSX Transportation for the year 2004.

Q. That's the number that was used in the proposed assessment for 2004?

A. Yes, sir.

Q. And just so the record is clear, would you read that number?

A.. 439 thousand, 58 thousand, 547.

Q. Is that 439 million?

A. Yes, sir, I'm sorry. 439 million, 58 thousand, 547.

Q. Now, is that 439 million dollar number derived from your unit value number of 10.767 billion?

A. No, sir.

Q. What is it derived from?

A. It is derived from the agreement, or settlement, whatever you want to call it, that the Department offered to propose to the various large utilities, including the railroads.

Q. Now, the 439 million dollar number reflected on that document?

A. Yes, sir.

[299] Q. You see what I'm talking about?

A. Yes, sir.

Q. That implies a unit value of how much?

A. I believe it was—I believe it was 6.5 billion.

Q. But not based on the unit value determination that you made for CSX for that year?

A. No, sir. That was not based on my valuation.

Q. But instead on this settlement or negotiations that you have just described?

A. Yes, sir.

Q. Now, when you decided in 2004 that the way in which you calculated your cost of equity needed to be modified, did that uniformly result in a cost of equity that would go down?
A. Yes, sir.
Q. How did that affect the 6.5, or how did that play in the 6.5 billion dollar number that was used for the proposed assessment for CSXT for 2004?
A. There is no connection.
Q. And that's why?
A. Because the 6.5 billion is not a number that I originated.
Q. That's a negotiated number?
A. Yeah. It is the number that the commissioner decided to base the 2004 assessment on.
Q. Now, let me ask you about 2004 and discussions that the [300] Department had with public utilities, including CSXT for that year. Were you part of those discussions?
A. Yes.
Q. Could you describe what meeting or meetings you attended?
A. I attended several meetings with the commissioner in which he indicated that he had been approached by several of the large Georgia utilities, who indicated that if my values were used, that they would be filing appeals for the year 2004.
Q. What did you anticipate that would mean in terms of additional litigation?
A. I guess at least, well, at least three from that, I would imagine, would have been more of 10 to 20.
Q. 10 to 20 tax appeals challenging the Department's proposed assessments?
A. Yes, sir. And that's just an assumption that they would kind of follow along with the big ones.
Q. Now, based on the information that the Department was getting from public utilities, was a meeting held with them?
A. Yes, sir, a meeting with Georgia Power, BellSouth, Atlanta Gas Light, Delta Airlines, and CSX Transportation,

Norfolk Southern Railway was held between those companies and the commissioner, and I attended that meeting. I can't remember if anybody else from the Department was in there, but I believe there was at least one additional person. The commissioner held that he had devised, I guess, well, he had [301] devised what he was going to offer these companies.

Q. Before you go on, let me just to make sure the record is clear. Is that a meeting that took place before the Revenue Department issued its proposed assessments?

A. Yes, sir.

Q. So the process, as I understand it, is that is that you prepare valuations or proposed valuations of the public utilities, and only after that point are the proposed assessments presented to the State Board of Equalization and then issued, is that accurate?

A. Could you repeat that, please?

Q. Sure. For example, looking at the document that is up on the screen, the 10.7, the 10.767 unit value for CSXT, that number was not used in calculating the proposed assessment for 2004, correct?

A. That's correct.

Q. Okay. Is that a number that you would have shared with CSXT at some point?

A. Yes. It was standard practice while I was working on the valuation work sheets, that particularly the major companies would want to come in and get sort of a preview, see if there was any information they could furnish that would change my opinion, and we discussed the value as to what that unit value ought to be.

Q. The process as you have described it, was that designed [302] to get the taxpayer's input as to your values before they were formalized in the way of a proposed assessment?

A. Yes, sir. It was an attempt to reach agreement prior to that point.

Q. So the meeting that you have been—that I have asked you about with sort of the public utilities, including the

railroads, that took place after you had come up with valuations of what you thought the unit values of these companies were, but before those numbers had been presented to the State Board of Equalization and put in a proposed assessment?

A. That's correct.

Q. Okay.

A. And let me go back to one of my answers. I'm not sure that that number was shared with CSX that year. I just can't remember whether we actually had discussions that year or not.

Q. Now, the meeting that we started to talk about, representatives of CSXT were at that meeting?

A. Yes, sir.

Q. Do you recall who was there on behalf of CSXT?

A. I believe it was David Boeing and Kerry Carnahan.

Q. And Mr. Carnahan holds what position at CSXT?

A, I believe he's a director of taxation. I believe it's more than just property taxation.

Q. Could that be a position of CSX Corporation at [303] the corporate?

A. Yes, yes.

Q. What were the discussions at that meeting?

A. I believe the commissioner did most of the talking. He started out the meeting expressing his concern with the level of disagreement, and that he basically wanted to—Well, he first started the meeting saying he wants to present these—some way of avoiding the litigation.

MR. MCBRIDE: This is all hearsay. He is telling us what the commissioner said.

MR. CALVERT: It's not for the truth of the matter stated. This is what the conversation was.

THE COURT: Right.

MR. MCBRIDE: It's not for the truth of the matter stated? I don't know where it's going.

THE COURT: I don't either, but go ahead.

Q. If you would, please.
A. Okay. The commissioner held, or started the meeting with saying — thanking everybody for coming, first, and said that basically the purpose was to see if there wasn't some way that the Department could avoid this onslaught of litigation, and give the parties additional time to discuss the issues, and see if some of the issues couldn't be resolved, and hopefully put that into place before the next year.

One of the things was that—The commissioner [304] basically asked the members present that if they agreed to go through this process, that any settlements reached would not be used for any purposes except this settlement and would not be used in prior or future litigation as binding.

MR. CALVERT: And before you go any further. Your Honor, the reason we are going into this at all is because Mr. McBride has brought up 2004. We agree that we don't think it is relevant. But since he's interjected it into the case, we want to make sure that it's clear on the record that what happened, the numbers that came out of the discussions for 2004 were compromise numbers. And that they were — and they don't indicate anything about where CSXT's true market value should be for 2002. So, I mean—

THE COURT: I understand your position.

MR. CALVERT: So I won't—We won't belabor this much, but I just wanted to make the record clear.

Q. What was the proposal that was made by the commissioner?
A. Basically, for the four members, well, I'm sorry, for the three members, other than the railroads, and Delta Airline, which isn't formed on the unit rule valuation, it's a plan by

plan valuation, that this year, that the 2004 Georgia taxable fair market value would be the higher of the 2003 Georgia taxable fair market value, or an average of the 2001, 2002 and 2003 Georgia taxable fair market value.

Q. Were those the values, when you say the 2003 or the prior [305] three years' taxable values, were those the values as they would have been accepted by the taxpayers for those years?

A. Yes, sir.

Q. Okay. Now, where did that—Were there any subsequent discussions with either of the two railroads as to how they could be included in that type of resolution for 2004?

A. Yes. As I remember, the other parties were dismissed. The representatives of the railroads stayed on. And there was—Well, during the whole meeting it was recognized that the railroads didn't have the three prior years of finalized values.

Q. And why is that?

A. Because 2002 and 2003 values were under appeal.

Q. By both railroads?

A. By both railroads.

Q. I say both railroads, you mean?

A. Norfolk Southern and CSX Transportation.

Q. Okay.

A. So the discussion ensued as to how to handle the two railroads in some equitable manner, some manner consistent with this prior three-year average. And the general guidelines when we left the meeting was that since the last agreed-upon value was 2001, that this number probably ought to consider some increase for time for the three years that had elapsed. Exactly what that number was wasn't settled at the meeting. [306] The railroads—Because of the time factor, this commissioner was very concerned with getting these—this digest out timely during July, and these meetings were in the middle of July. The proposed values for the other utilities was presented to them at the meeting. The two railroads were

requested to go back, come up with a number, with a suggestion that it be the 2001 plus some increase for time, and to respond back to the Department. And I forget, I think this was early to mid week, respond back by the next Monday as to what that number would be, what they could agree to, so that we could turn around and turn out this digest the next day. Norfolk Southern responded, I believe, that Friday, and proposed a number. The number was basically the same as the 2001 value, and I guess I made the decision that that was good enough.

Q. What about CSXT?

A. CSXT did not respond, and I was left to a comment I had heard at the meeting, I believe made by Kerry Carnahan, that something in the area of 6.5 billion might be reasonable.

Q. Or would be acceptable to CSXT?

A. Again, I don't think Kerry or anyone was agreeing at the meeting, but he was sort of presenting it as something he thought his management would agree to. When I didn't get a response by noon Monday, I think the deadline was, in order to get the numbers crunched through the system, and get the assessments out, or get the digest to the board the next day, I [307] used the 6.5 as a basis for the 2004 assessment.

Q. Did CSXT appeal that assessment for 2004?

A. No, sir.

Q. Mr. Dickerson, I'm going to quickly go through a few points that were touched on by Mr. McBride in his questioning of you. You have—At different times during your testimony we have referred to your full appraisal or your complete appraisal as distinguished from the document which I believe is plaintiff's exhibit 32 and defendant's exhibit 13. Why do you distinguish those two documents in the way you refer to them?

A. Well, mainly it's the narrative portion. The distinction—There is a distinction between the amount of effort that goes into it, but the main difference is the narrative that you would include within an appraisal, whenever you are going to turn

an appraisal over to a client. Typically, since I am my own client, I guess, we don't prepare narrative appraisals. We only go through the valuation work sheets. Now, depending on the scope of the research you have done prior to that, that could be a preliminary number. But as the appraisal, as both appraisals show, I mean, the valuation work sheets later serve as an addendum to the narrative appraisal, and the narrative appraisal merely refers to sections within that valuation work sheet.

Q. Now, Mr. Dickerson, how many unit valuations have you performed—have you performed during your professional [308] career?

A. Well, I would perform—

MR. MCBRIDE: I want to be sure I understand what he means by valuation. We have an issue about that. If he could just explain what he means by valuation.

MR. CALVERT: I'll do that, Your Honor.

THE COURT: All right.

Q. How many companies have you valued using the unit rule?

A. I would guess it's approximately, today, it's probably 150 companies a year. It would have been—and that's probably true for the last three years. In my ten prior years at the Department of Revenue, that number was probably more like 110 to 120, the difference being the large increase in the number of telecom companies.

Q. So 120 to how many a year?

A. 120 to 150 a year.

Q. That would be a rough estimate of the number of companies you have valued under the unit rule during your entire professional career?

A. Yes, it would be that times thirteen years, I guess.

Q. Okay. Now, there was also some discussion during your testimony earlier today about a range of fair market value

versus a point estimate of fair market value. Could you explain again the—or explain for us now the difference between those concepts?

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IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

No.1:02-CV-2634

CSX RAILROAD TRANSPORTATION, INC.
Plaintiff,

vs.

STATE BOARD OF EQUALIZATION,
Defendant.

TRIAL TRANSCRIPT

VOLUME III - MAY 18, 2005

BEFORE THE HON. CHARLES A. PANNELL, JR.

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WITNESS	DIRECT	CROSS	REDIRECT	RECROSS
Thomas Tegarden	368	429	514	

* * * *

[369] Q. Do you hold any appraisal designations?
A. Yes, I do.
Q. What are they?
A. I hold the MAI appraisal designation from the American Institute of Real Estate Appraisers, now known as simply The Appraisal Institute, and it is considered the highest appraisal designation offered in the field of appraisal. I also hold the CAE, Certified Assessment Evaluator, from the International Association of Assessing Officers, it is also the highest designation offered by that organization as well. I also am a Tennessee Certified General Appraiser and a licensed appraiser, and I also hold licenses similar to that in the states of Michigan and Minnesota.
Q. How long have you been doing this appraisal work?
A. A little over thirty-five years.
Q. In doing this appraisal work, do you always represent utility companies?
A. No, sir.
Q. What other kind of entities do you represent?
A. Well, we do appraisal work, consulting work, property tax type work for both sides of the property tax paying spectrum. We have clients, for example, the Wyoming Department of Revenue, we have worked for the New Hampshire Department of Revenue, the Florida Department of Revenue, Georgia Department of Revenue, Colorado Department of Revenue, South Dakota [307] Department of Revenue, and Dallas County, Texas, Anchorage, Alaska, Valdez, Alaska, just various tax administrative organizations.
Q. All right. That's fine. And you—In addition to those, I take it you represent companies like CSXT here?
A. Yes, sir, we do.
Q. Do you represent companies like BellSouth?
A. BellSouth, AT&T, Quest, Southwestern Bell, Georgia Power.

Q. And you do that work on an annual basis for them, is that right?

A. Yes, sir.

Q. Okay.

A. As a rule, that's correct.

Q. Now, you said you did some work for governmental agencies. Could you describe for me generally what kind of work you do for governmental agencies?

A. Well, the same type that we do for property taxpayers. A lot of times for governmental agencies, we will speak to legislators, or speak before legislative committees, or teach public utility basic appraisal courses, etcetera. That's one of the things we do a lot of for state departments of revenue.

Q. And when you teach, do the state people come to those courses?

A. State people, as well as property taxpayers, and judges, legislators, various individuals that are interested in this [371] field.

Q. In addition to teaching in those kind of situations, do you have an occasion to teach appraisal of utilities in some other context?

A. Yes. For the Wyoming Department of Revenue, we actually wrote an appraisal course that we have taught to several different departments of revenue around the country, and we go out there annually as a rule and teach, put on a course that we limit to twenty-five students from around the country on a first come first serve basis, and teach them basically the appraisal principles involved in ad valorem tax valuation of public utilities and railroads.

Q. And do you ever attend the Wichita Workshop?

A. Yes, sir. I have attended every one of them. There has been something like, I think, thirty-four of them now and I have attended all of them, and have taught at most of them.

Q. What's the Wichita Workshop?

A. The Wichita Workshop is a workshop at the Wichita State University that is dedicated specifically to the ad

valorem tax valuation of public utilities and railroads. It's attended by probably 400 to 500 people a year from around the country that are interested in this field, tax administrators as well as taxpayers, and occasionally judges and legislators, that sort. But it's the only workshop of its kind really that's dedicated to this type of work that's sponsored by a state university, [372] and is put on with all types of people coming to it regularly and in large numbers.

Q. Mr. Tegarden, before you began Thomas Tegarden and Associates, what did you do?

A. For fifteen years I worked at the Tennessee Public Service Commission, and the Tennessee Public Service Commission was one of two commissions in the nation that did the ad valorem tax valuation of public utilities and railroads in addition to setting their intrastate rates. I worked as the assistant director of assessments there for about eleven of the years, and all totaled I worked there for fifteen years before I started my own appraisal business.

Q. So you have been in your own appraisal business for what, about twenty years?

A. Twenty-two, twenty-three years, yes.

Q. Okay. All right. I want to see if we can try to get—put this case in perspective, and I want to talk a little bit about appraisal. And I want to take a little bit of time, if we can this morning, to kind of go through the appraisal process and talk a little bit about appraisal principles and the unit assessment. First, is your objective in this case to determine the market value of property?

A. Yes, sir.

Q. And what definition of market value do you use?

A. Well, we list it on the very first page of our appraisal,

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IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

No.1:02-CV-2634

CSX RAILROAD TRANSPORTATION, INC.
Plaintiff;

VS.

STATE BOARD OF EQUALIZATION,
Defendant.

TRIAL TRANSCRIPT

VOLUME IV - MAY 19, 2005

BEFORE THE HON. CHARLES A. PANNELL, JR.

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Judith Ross	520	536	573	
Kerry Carnahan	574	587	618	620

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* * * *

[578] strategic plans, or any budgeting information, or anything like that in our annual filings.

Q. Okay. So you are familiar with what other states were doing for CSXT in 2002, which is the assessment year, correct?

A. Yes.

Q. Now, Mr. Dickerson said that he was trying to find the lowest estimate of value he could come up with, his 8.2.

MR. CROSSETT: I object to the form of the question, Your Honor. Mr. McBride is trying to characterize testimony from another witness.

MR. MCBRIDE: I'll rephrase my question, Your Honor.

THE COURT: All right.

MR. MCBRIDE: I'll just ask you very quickly.

Q. Of the fifteen states that you have that do a unit value, is Mr. Dickerson's value the lowest?

A. No, it's not.

Q. Is it the highest?

A. It exceeds the highest, yes.

Q. All right. Thank you. Now, I want to talk to you very quickly—I want to talk to you just very quickly about the Georgia assessment. Do you have a copy of exhibit 8 with you, Mr. Carnahan?

A. I do.

Q. Okay. And did you at my request prepare exhibit 8?

A. I believe I did, yes.

* * * *

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

No.1:02-CV-2634

CSX RAILROAD TRANSPORTATION, INC.
Plaintiff,

VS.

STATE BOARD OF EQUALIZATION,
Defendant.

TRIAL TRANSCRIPT

VOLUME V - MAY 20, 2005

BEFORE THE HON. CHARLES A. PANNELL, JR.

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WITNESS	DIRECT	CROSS	REDIRECT	RECROSS
Hal Heaton	683	699		
James Bicksler	740	756		
Gregg Dickerson	764			

* * * *

[765] Q. Now, Mr. Dickerson, I have handed you what's been marked and admitted at defendant's exhibit 14, and if you will turn to addendum E to that document.

A. I have it.

Q. And can you tell me, does addendum E accurately describe your professional experience and training in the field of property valuation?

A. Yes, it does.

Q. And would you briefly take us through that, please?

A. Basically as far as formal education, I received my BSED degree in math education from the University of Georgia in 1972, as far as education. I taught for a year, then joined the Department of Revenue and was sent to a training course in all aspects of real estate appraisal that was like, I think, an eight to ten week course.

Q. Now, you said the Department of Revenue. Is that the Department of Transportation?

A. I'm sorry, Department of Transportation. Thank you. Upon completing that course, I subsequently challenged or took and passed the American Institute of Real Estate Appraisers exams for course 1, course 2—I'm sorry, course 1A, which is basic appraisal theory, course 1B, which is an introduction to the income approach, and course 2, which is the advanced income approach.

Q. Now, how long were you employed by the Georgia Department [766] of Transportation?

A. Approximately ten years.

Q. And that was as an appraiser?

A. Yes, sir. I started as a right-of-way appraiser 1. At the end of the term, I was a right-of-way acquisition team leader, which just meant that I—besides preparing appraisals, I was responsible for an acquisition team that handled both the appraisal and acquisition of needed right-of-way parcels.

Q. Approximately how many property valuations did you perform while you were with the Georgia Department of Transportation?

A. Several hundred. Typically, a right-of-way acquisition project will have maybe fifty to a hundred parcels, of which there may be one or more appraisers assigned to. It would be hard to put a number on those.

Q. Now, how long were you with the Georgia Department of Transportation?

A. Ten years.

Q. And after that, where did you go?

A. I joined—I went with the Georgia Department of Revenue as the Public Utility Valuation Manager.

Q. And you were hired to do then essentially what you are currently doing now?

A. Yes, sir.

[767] Q. You were hired by Ms. Judith Ross?

A. That's correct.

Q. And what year was that?

A. That would have been about approximately 1983.

Q. Now, what I will refer to as your first stint with the Revenue Department lasted from about 1983 until when?

A. 1993, approximately ten years.

Q. Now, during that ten-year period, were you involved in property valuations?

A. I would say the first year I was involved in property valuations. When I noticed what the Department was doing at that time, it became—and upon studying what the unit rule meant, it became apparent that the Department was not doing the unit rule as I perceived it, which was basically to value the business. And so during that first year, I was changing the way that the Department did it, so by the next year, I would call what I did from that point on business valuations.

Q. Under the unit rule?

A. Yes, sir.

Q. And approximately how many of those types of valuations did you perform before you left the Revenue Department?

A. I would say over the ten-year period, over a thousand.

Q. Now, you have been here during all the testimony in this trial so far, haven't you?

A, Yes, sir.

[768] Q. Did you hear Mr. Tegarden testify regarding the Wichita workshops?

A. Yes, sir.

Q. Tell us again, would you, what the Wichita workshops are.

A. Basically the Wichita workshop, it is sponsored by the National Tax Association and Wichita State University. It is, I believe, the largest gathering of this type for people involved in this field. It's attended by both state administrators, company tax representatives and tax consultants. And it serves as sort of an exchange of ideas. The program, they attempt to keep it balanced, and normally a program, there will be segments on particular issues that are in, I guess, in controversy. And the program will attempt to have one person that represents each side of a particular controversy and present those to the audience.

Q. Do the topics that are covered include the various valuation methodologies that should be used in arriving at unit valuation of public utilities?

A. Yes, sir, they do. They cover all the approaches. They even have had segments on allocation, some of the minor issues. But the programs do tend to focus on the income approach and market approaches, as those are sort of the sources of the main controversies.

Q. Now, I think you mentioned, how often have you attended that conference?

[769] A. I attended it, I believe, out of the past twenty, twenty-one years, I have missed that conference twice, as of now.

Q. Now, have you also been a presenter at that conference?
A. Yes, sir. I have been a frequent presenter on the main program. Again, most of the topics that I presented have been regarding the income approach, or the market approach, and did one year assist Mr. Tegarden in the presentation of the basic course, I think, trying to remember, I think as my segment of that, I think I presented the cost approach.
Q. And as it applied in the unit value context?
A. Yes, sir, and as written in that course.
Q. So you and Mr. Tegarden were like co-presenters or co-panelists?
A. Mr. Tegarden is in charge of the basic program out there, and I was just asked to present a small part of it.
Q. Were you asked by Mr. Tegarden to do that?
A. I really don't think it was directly from Mr. Tegarden. Again, the planning committee likes to vary the presenters even within the basic course, just to get sort of new blood into that program.
Q. Now, have you taught unit rule valuation methodologies in any other settings?
A. Yes. During my first stint with the Department of Revenue, I developed and taught a course for two years on the [770] valuation of public utility properties. It was taught to the—during what the Department calls a short course, which is a week-long session held at the University of Georgia, where various courses are taught both by Department people, and I believe they also teach IAAL courses for the local assessors.
Q. Are you also published in your field?
A. Yes. I have—Well, I have been published in the property—let me see here. Been published in the "Appraisal Journal," the "Assessment Digest," and the "Property Tax Journal," which are monthly publications. The first one is one of the, I believe, published by the American Institute of Real Estate Appraisers. That, of course, didn't deal with unit valuation, it dealt with, at the time, it was a time during which

there was some creative owner financing going on, and it was a method of adjusting for that creative financing.

Q. Those publications that you mentioned, are those national publications?

A. Yes, sir.

Q. Now, you have testified that you were with the Revenue Department from I believe 1983 to 1993, is that correct?

A. That's correct.

Q. What did you do after that? Where did you go?

A. In 1993, I was employed by Norfolk Southern Corporation as a property tax manager.

Q. Now, when did you return to the Revenue Department?

[771] A. I returned late 2001.

Q. Were you approached by the Department?

A. Yes, sir.

Q. And who approached you about returning?

A. Well, I was approached several times by Mr. Joseph Slappy, who was doing this job, basically. He was more or less pleading with me to come back, that he no longer wanted to do this job. And then on one of my visits to the Georgia Department of Revenue, Mr. Larry Griggers, who we [sic] the director of the Department at that time, called me into his office, asked if I would be interested in coming back, and we talked about it.

Q. What did Mr. Griggers tell you he wanted you to come back and do?

A. He expressed a concern what had been happening as far as the valuation of public utilities since I had left. His concern was that he had looked at the digest through that period and had noticed that the public utility digest when I left was approximately 10 percent of the total state property tax digest, and had fallen to about 5 percent of the total digest.

Q. Did you suggest anything that you could do to correct that situation?

A. I expressed interest in returning, although I told him if his interest was in raising the numbers, I would not come

back [772] for that purpose. If his interest was in getting it right, I would be interested in returning, if he could come close to matching my salary where I was.

Q. Did Mr. Griggers match your salary and your conditions?

A. He matched my conditions, and he came close to matching my salary.

Q. All right. Now, when did you actually return to the Revenue Department?

A. I believe it was either August or September of 2001.

Q. So were you involved at all in the setting of the public utility proposed assessments for the tax year 2001?

A. No, I was not. And I believe at that time it hadn't been presented to the State Board, but Mr. Griggers desired that I not become involved in that digest, so that I could have a clean start in 2002 and not be tied to anything the Department had done prior to that.

Q. But you were involved in setting values for 2002, correct?

A. Yes, sir.

Q. And it was solely your responsibility to do the valuations that led to the proposed assessments for 2002?

A. That is correct.

Q. Now, after you came back to the Revenue Department and began to review the methods that were being used, or how they were being applied, what changes, if any, did you make?

[773] A. Well, the Department at the time was doing a yield capitalization in a form that is commonly called today capitalized earnings, where you convert a first year's estimated free cash flow by a cost of capital minus growth rate. They were also doing what was labeled as a direct capitalization method, where they were using the band of investment similar to the method used in the weighted average cost of capital to combine things like a EP ratio, the inverse of PE ratio with a cost of debt as being—that

representing a direct relationship between earnings and price, and they were doing a stock and debt.

They were basically—These approaches, I think that I instituted, replaced those. They are, I guess, theoretically comparable, but they are the form that is commonly used in business valuation. I replaced the discounted earnings, I'm sorry, capitalized earnings approach for the discounted cash flow; replaced what has been labeled as direct capitalization with the market multiples approaches, and kept the stock and debt.

Q. And why did you institute those changes?

A. During my absence, I had the opportunity to look at a great many documents. I was at Norfolk Southern when the Conrail merger or acquisition took place. I was able to review the procedures that were done by the various providers of fairness opinions in that transaction, and it was my desire to [774] replicate the method actually used in the marketplace.

Q. To arrive at values?

A. To arrive at values.

Q. Now, did you make any changes in terms of what type of income figures or data were used in performing these methodologies?

A. Yes. There are—The state of Georgia, like most states, have historically relied on regulatory reports as our sources of income information and cost information. I found out, again, while working at Norfolk Southern that investors in the railroad case, at least, rarely even know what an R1 is. It's not something that they look at in determining their analysis of a railroad company.

They look at the annual reports to stockholders, the 10K's filed with the Securities and Exchange Commission. That was the type of information they were interested in, and, again, to replicate the actions of the market, I thought they were a better source of income information.

Q. So in doing your railroad valuations for 2002, did you change from using R1 type of data to using data from another source?

A. Yes, sir. I changed to using the—what's reported in their annual reports as the rail segment.

Q. Now, you testified earlier this week concerning the 2002 public utility digest, and the increase in value that CSX [775] experienced from 2001 to 2002. Do you recall that testimony?

A. Yes, sir.

Q. Can you give us a general idea of what accounted for that increase in value?

A. Of course, there would be a difference in the markets from one year to the next, but in terms of this case, a big driver of the difference was the change in the source of the income information.

Q. And that's the change from R1 data to annual report data?

A. Yes, sir.

Q. Mr. Dickerson, I have handed you what have been admitted into evidence as joint exhibit 2 and joint exhibit 11, and if you will look at joint exhibit 2 first and tell me what that document is.

A. This is the 2001 annual report to stockholders of CSX Corporation.

Q. Now, is that a document from which you would have gotten income figures used in determining your values for 2002?

A. Yes, sir, it is.

Q. Now, if you will turn to page 18 of that document. Have you found that page?

A. Yes, sir.

Q. And tell me, what income numbers would you have been looking at on this chart at the bottom of the page?

A. Okay. I basically would have been looking at all the [776] numbers in the left hand most column under the heading, rail. I would have used that as source of revenues,

expenses, and calculated from that an offering or net revenues from railway operations as the term is in the RI's, but here it is called operating income. That would have been—Of course, as I went through the expenses, there is a 60 million dollar charge for the New Orleans litigation, which is a type of special charge or non recurring charge that I would have eliminated.

Q. But the line here for operating income, 746 million dollars, see that?

A. Yes, sir.

Q. That's the operating income indicated on this document for the rail segment of CSX Corp.?

A. That's correct.

Q. Is that basically the income number that you are going to be working from?

A. Yes, sir.

Q. Okay. If you will keep that page open. And if you will look at joint exhibit 11, CSXT's R1 report for 2002, and if you will find page 16 of schedule 210. Have you found that?

A. I have it, sir.

Q. See if I can make this work. Okay. Now, can you point to us—point to the line that shows railway operating revenues on this R1 report.

A. Yes, that would be line 13. If you will come across to [777] the amount for the current year, would be the 6,082,282,000.

Q. And what's the corresponding number on the annual report?

A. 6 billion 82 million.

Q. So it's the same number?

A. Yes, sir. In the annual reports, they round to millions. RI's, they round to thousands.

Q. Now, on the R1 report, would you direct us to the line which shows the total railway or the railway operating expenses?

A. Yes, sir. That is line 14, and, again, if you follow that over to the first column, that would be the amount for the current year, the 5,623,637,000.

Q. Now, what's the comparable number on the annual report?

A. On the annual report, the annual expenses are 5 billion 339 million.

Q. So on the R1 report, what is the amount shown for net revenue from railway operations?

A. That would be 458 million, 645 thousand.

Q. And that is basically line 13 minus line 14, correct?

A. Yes, sir, and shown on line 15.

Q. So that's 458.6 million dollars?

A. Yes, sir.

Q. And how does that compare with the operating income shown for the rail segment on the annual report?

A. On the annual report, that's 743 million, a difference of [778] roughly, well—

Q. Right around 285?

A. 285 million.

Q. Okay. So, just so it is clear, the operating income numbers that you worked from for 2002 would have been reflected in the 743 million dollar figure on the annual report, correct?

A. That's correct.

Q. As opposed to the net revenue from railway operations of 458 million dollars shown on the R1 report?

A. That's correct.

Q. Now, explain again why you decided to go with the figures on the annual report instead of the R1 report.

A. Again, the R1 is a regulatory report. It was my observation while at Norfolk Southern that investors don't look at and in most cases don't even know that that report exists.

Q. Now, had you been employing the same methods or techniques for 2002 that the Department had been using for 2001, which income number would you have used?

A. I still would have used the numbers out of the annual report.

Q. Perhaps I didn't make it clear. If you had been—perhaps the way to put it better. If your predecessor had been applying the technique for 2001, the same technique he used in 2001 to determine the 2002 valuations, which number would he have been looking at?

[779] A. I assume, since he hadn't made any changes during his tenure there, that he would have used the numbers out of the R1.

Q. Which would be the 458 million dollars?

A. That's correct.

Q. And very quickly, I'm going to hand you joint exhibit 1 and joint exhibit 10, and we are going to look at the same numbers for 2001. If you will look at joint exhibit number 10. First, you recognize that as the R1 report for CSXT for 2000?

A. Yes. This is the R1 for the year ending December 29th, 2000.

Q. If you will find page 16 of schedule 210 on that document. You see that?

A. Yes, sir.

Q. Okay. Again, point out the pertinent data on that R1 document, or the data that the Revenue Department would have been using for 2001.

A. Yes. Again, we would be working off the net revenues from railway operations.

Q. And that's line 15?

A. Line 15 in the R1, that is 323 million—well, 323.9 million.

Q. Okay. Now, on the annual report for that year, if you will turn to page 16.

A. I have it.

[780] Q. And what is the—I'll say comparable figure. It's not comparable, but what is the—what's the figure shown here for operating income for the rail segment on the annual report?

A. The corresponding number is the operating income of 615 million.

Q. Okay. And, again, is the difference between these, the numbers shown on the annual report and the numbers shown on the R1 report what those respective documents report as operating expenses?

A. It reflects what their operating expenses were reported, yes.

Q. So for regulatory purposes, CSXT is showing the same operating revenue both on the R1 as it is showing for the rail segment in the annual report, correct?

A. That is correct.

Q. And the difference is for regulatory purposes on the R1, it is showing larger, and significantly larger, operating expenses than is reflected on the annual report for the rail segment?

A. Yes, sir.

MR. CALVERT: Ms. Martin, could I get plaintiff's exhibit 32?

Q. Now, I have handed you a document we have talked about a little bit already in this proceeding, and I will try not to belabor the testimony about it, but I want to make sure the

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IN THE UNITED STATES DISTRICT COURT FOR THE
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

CAUSE NUMBER 1:02-CV-2634

CSX RAILROAD TRANSPORTATION, INC.
Plaintiff,

VS.

STATE BOARD OF EQUALIZATION,
Defendant.

TRIAL TRANSCRIPT

VOLUME VI - MAY 23, 2005

BEFORE THE HON. CHARLES A. PANNELL, JR.

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Carolyn Sizemore	882	915		
Fredrik Eliasson	919	977	984	

• • • •

[886] Q. The company wouldn't expect to see that type of charge on an ongoing basis?
A. Would not.
Q. Would not.
A. That's right.
Q Ms. Sizemore, I have handed you what has been marked as joint exhibit 8, and can you identify that document?
A. It is the CSX Transportation's 2001 form 10K.
Q. CSXT and CSX Corp. file separate 10K's, correct?
A. That's right.
Q. This is the one for T?
A. That's right.
Q. Can I get you to turn to page 12 of that document? Is that the same page I have got up on the screen?
A. Yes, it is.
Q. Now, the operating income shown on this document of 459 million is different from the operating income shown on the 2001 annual report for the rail segment, correct?
A. That's right.
Q. So, is it correct to say for 2001, CSX Corp.'s management would not have viewed the performance of the company's rail segment as being reflected by the 459 million dollar operating income shown on the 10K for CSXT?
A. That's right.
Q. Now, I have handed you joint exhibit 11. Can you [887] identify that document?
A. It is the Ri report for CSX Transportation for the year 2001.
Q. Now, if you could take a moment and find page 16, schedule 210.
A. Okay.
Q. Now, if you will look at line 15 on that page, which shows net revenue from railway operations, 458 plus million dollars. Do you see that line?
A. 458 plus—What did you just say?

Q. 458 million.
A. Oh, I have got you.
Q. Plus?
A. It's billions, because this is in thousandths.
Q. The net, on line 15?
A. Right.
Q. That's 458 million 645 thousand, correct?
A. Yeah, I'm sorry, that's right.
Q. Now, that's essentially the number that is shown on the 10K for CSXT's operating income, correct, the 458 million?
A. I actually would need to spend some time with this document to compare those two.
Q. But the amount is essentially the same?
A. It looks like the same amount rounded.
Q. Well, let's look at it a little more closely. The amount [888] on this document, which is shown for—on line 10 for railway operating revenues, which is 6.082 billion, you see that amount?
A. I'm sorry. Can you repeat the question?
Q. Yes, on line 10. It shows railway operating revenues of 6.082 billion.
A. Uh-huh.
Q. See that?
A. Yes.
Q. That's the same amount that is shown as operating revenues on the 10K for CSXT, correct?
A. Okay, yes.
Q. Okay. And the railway operating expenses on line 14 of the R1 are 5.623 billion dollars. You see that number?
A. Yes.
Q. That's the same operating expenses as shown on the 10K for CSXT, correct?
A. That's correct.
Q. So it would be fair to assume then that the net revenue from railway operations shown on the R1, which is just the

difference between the expense number—the revenue number and the expense number is the same as the operating?

A. Yes.

Q. On the 10K?

A. Yes.

[889] Q. As a consequence, the 458 million dollar number shown as net revenue from railway operations on the R1, would also —that would not be reflective of management's view of the operating performance of CSX's rail segment?

A. This is not talking about the rail segment. This is only talking about CSX Transportation legal entity, so different rules govern this report, and you don't have to show this report in those same segments that the SEC requires.

Q. I understand that, but as a consequence that number on line 15 would not reflect the management's view of what the operating performance of the rail segment is?

A. I would not be comfortable saying as a consequence. That's not how the company views performance at the railroad.

Q. Did you say you would not. Could you read that answer back, please?

(Record read as requested)

Q. Would you agree that to the extent that the net railway from railroad operations number is a different number than the operating income that is shown on the rail segment of the annual report, that to the extent there is a difference between those numbers, management's view of how you measure the operating performance of the rail segment is the number shown in the annual report and not the R1?

A. The R1 is a conglomeration of a different set of rules and numbers that are used to prepare this statement and they [890] don't have to abide by segment reporting, okay? That doesn't mean that management doesn't use these numbers in any way. If you go to the 10K, the CSX Corporation where

we show the rail segment, there are very specific rules for all public companies on how you show and define each segment that you have within your business. So the R1 is a very industry specific document comparing data from all different railroads. I'm not comfortable saying management doesn't rely on information on how the business is doing in the R1.

Q. But let me review your testimony from just a short time earlier. It is your testimony that the operating income number that is shown on the CSX Corp.'s annual report for the rail segment would represent management's view of how you measure the operating performance of the rail segment, correct?

A. That's correct.

Q. So if that number is different from what is shown on the R1, the R1 does not reflect management's view of how you measure the operating performance of the rail segment?

A. And I'm not comfortable connecting those two dots. This is a totally different document. It is a legal entity, CSX Transportation. It is a different set of requirements and rules that are needed. So I'm not saying that the company doesn't rely on information in this report on how the company is operating.

Q. And that's not—that is not my question as to whether [891] the company relies on the R1 numbers in some fashion or not. But it is your testimony that the numbers—the operating income numbers shown on the annual report for CSX Corporation's rail segment reflect management's view of how you measure the operating performance of the rail segment, correct?

A. Yes.

Q. But you are not comfortable in saying that if the R1 numbers are different from that, that the R1 does not reflect management's view of how you measure the operating performance?

A. No. Why don't you ask me the question again. I'm getting confused by your questions.

Q. The annual report showing the operating results of CSX rail segment, the operating number that is shown on the annual report for the rail segment is reflective of management's view of how you measure the operating performance of the rail segment, correct?

A. That's right.

Q. Okay. If that number, if the net railway operating expense, net railway from railroad, sorry, if the net revenue from railway operations on the R1 report is different from what the annual report shows for the rail segment, then the R1 report does not reflect management's view of the operating performance of the rail segment.

A. The R1 report is not the rail segment, so it's totally different documents.

[892] Q. So you can't evaluate the operating performance of the rail segment based on the R1 report?

A. Not of the rail segment. This is just CSX Transportation, which is specifically the railroad.

Q. Whereas the rail segment on the annual report would represent all the rail transportation that are owned or used in providing rail freight service by CSX Corp.?

A. That's correct. It's a different—legal entities that add together to get to the rail segment.

Q. Ms. Sizemore, I have handed you what's been marked as joint exhibit 5. And can you identify that document?

A. It is the financial supplement for CSX Corporation in 2001.

Q. If you will turn to page 3 of that document. I'm sorry, that is the wrong page. It's not page 3. Now, that is page 3 of the document I have just handed you.

A. Yes.

Q. And, I'm sorry, did you identify that document?

A. Yes, I did.

Q. And that's the financial supplement to the 2001 annual report, correct?

A. That's right.

Q. Now, this document also reflects a segment reporting, doesn't it?

A. This is not governed by the SEC rules. It's additional

* * * *

[1037] percent terminal growth rate and change it to 3.7 percent growth rate, that's going to drive—that's going to come up with a lower terminal value than the one you chose up there, correct?

A. That's correct.

Q. And if you took the lower of the four terminal values so calculated, you would choose the one with the 3.7 percent terminal growth rate, correct?

A. Yes.

Q. If you did that, would that give CSXT a benefit in setting their value that none of the other unit value companies got?

A. I would say so.

MR. CALVERT: That's all, Your Honor.

MR. MCBRIDE: We have nothing, Your Honor.

THE COURT: Let me make sure of something.

MR. MCBRIDE: We move in 66, please,

MR. GOODWIN: Your Honor, I have already given it to Ms. Martin.

THE COURT: It is in. Let me ask, let me make sure. On the valuation work sheet, exhibit 32, page 1, up at the top, how did you choose the 8.2 billion as your proposed unit valuation of CSXT?

THE WITNESS: It's hard to back track as to how I did it. But basically, I had the range of the multiples from the [1038] multiple study. I could pick, as a for instance, the lowest indicated multiple of revenues. I could pick the lowest indicated multiple of E-B-I-T-D-A. Those numbers are not on

this sheet. But that helped me set what I thought was the lowest reasonable estimate of fair market value. It helped that I could construct a discounted cash flow analysis that came out with a similar number. If I hadn't been able to come up with a discounted cash flow, making conservative estimates that was at the bottom of the ranges of these market multiples, it could have been high, the point there, the lower limit would have been higher. But basically it's my belief that the market multiples, if you go to the extremes of either end, that those set the range and you can't go out of that range.

THE COURT: What weight did you give the discounted cash flow approach?

THE WITNESS: I don't do weighting [sic]. Again, the true value to me of the discounted cash flow is to help you narrow the range, or to arrive at a point estimate. When sort of your target is setting this range so that you can choose a lower limit to it, I think you are more relying on the market multiple approaches.

THE COURT: All right. So we are talking about the market multiple approaches. Where are the calculations to give me the range?

THE WITNESS: I think it's, depending on the order, it [1039] could be the third page where it says—it's half a page of printing, Comparable Publicly Traded Company Analysis.

THE COURT: And that's going to give me the range?

THE WITNESS: No, that is going to give you the point estimate for each of those, applying each of my point estimate of each of the multiples. As far as the range of all, as a for instance, the range of all the revenue multiples from the study, you would go to the next to the last page that's captioned Market Multiples at the top.

THE COURT: All right.

THE WITNESS: And, again, as a for instance, you could

look at revenues, and for these six railroads, sort of an absolute starting range would be the lowest of 1.66 to a high of 3.25. I mean, it depends on how much you want to refine the range, but that's a starting point as being sort of the absolute. Well, I don't want to say the word, absolute, because if there was something unusual about the company you are appraising, you could go outside of that range.

THE COURT: All right. And there is no weight to your various approaches, you are just comparing them?

THE WITNESS: I think that's true.

THE COURT: To come up with the 11.

THE WITNESS: I mean, it's really looking at all of them. It's really looking at all of them. But, again, your answer has to make sense in terms of all the approaches. I [1040] think I mentioned the—what I consider to be the most—one of the most important sheets in there is the sanity check at the end, where whatever number you picked, you would calculate what multiple did that indicate, or what percentage of the whole stock and debt that was. An appraisal has to make sense.

THE COURT: Any other questions for this witness?

MR. CALVERT: No, Your Honor.

MR. MCBRIDE: No, Your Honor.

THE COURT: All right. He can step down. Call your next witness. No, we are going to stop. All right. 9:15? See you in the morning.

(Trial recessed for the day)

UNITED STATES DISTRICT COURT
N.D. GEORGIA
ATLANTA DIVISION

Civil Action No. 1:02-CV-2634-CAP

CSX TRANSPORTATION, INC.,
Plaintiff,

v.

The STATE BOARD OF EQUALIZATION of the State of Georgia; BART L. GRAHAM, Commissioner of Revenue of the State of Georgia; RUSSELL W. HINTON, State Auditor of the State of Georgia; and RAY J. CRAWFORD, Director of the Georgia State Properties Commission,
Defendants.

Sept. 29, 2005

ORDER

PANNELL, *District Judge.*

The plaintiff, CSX Transportation, Inc. ("CSXT") filed this suit under Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976, Pub.L. 94-210, 90 Stat. 54 (Feb. 5, 1976), which is now codified at 49 U.S.C. § 11501 (the "4-R Act"). The 4-R Act confers concurrent jurisdiction on federal district courts to enforce its provisions, so long as "the ratio of assessed value to true market value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." *Id.* § 11501(c). Such jurisdiction lies notwithstanding the Tax Injunction Act of 1937, 28 U.S.C. § 1341, which ordinarily

prohibits district courts from enjoining, suspending or restraining the assessment, levy or collection of taxes under state law where the party may have a plain, speedy, and efficient remedy in state court. *Id.; Southern Railway Co. v. State Board of Equalization*, 715 F.2d 522, 526 (11th Cir.1983).

For the 2002 tax year, the Department of Revenue of the State of Georgia (the "Department") determined that the unit value of CSXT's rail transportation property was $8.2 billion and that the fair market value of CSXT's taxable railroad operating property in Georgia was $514,862,671 (the "Proposed Valuation"). The Department presented that value to the State Board of Equalization for the State of Georgia (the "Board") for approval. The Board approved the Proposed Valuation and issued a Notice of Proposed Assessment dated November 25, 2002.

CSXT makes three claims under the 4-R Act based on the Department's Proposed Valuation. First, CSXT claims that the Proposed Valuation is excessive and discriminatory in that the Department assessed CSXT's rail transportation property for ad valorem tax purposes at a higher ratio of assessed value to true market value than the ratio applicable to other commercial and industrial property in Georgia in violation of 49 U.S.C. § 11501(b)(1). Specifically, CSXT claims that the true market value of its rail transportation property on a unitary basis for the 2002 tax year does not exceed $6 billion, and that the true market value of its taxable rail transportation in Georgia does not exceed $369,253,752. This valuation claim is based primarily on an appraisal done by Mr. Thomas Tegarden, whose credentials are impeccable.

Second, CSXT claims that it has been singled out for discriminatory tax treatment by the defendants for the tax year 2002 in violation of 49 U.S.C. § 11501(b)(4). In particular, CSXT claims the Department's assessment of other centrally-assessed property is not based on the fair market

value of those properties. CSXT also claims that it is the only major centrally-assessed taxpayer in Georgia that suffered a significant tax increase for the tax year 2002.

Third, CSXT contends that the defendants discriminated against it in violation of 49 U.S.C. § 11501(b)(4) because the Department's Proposed Valuation for the tax year 2002 improperly included its intangible property, while the intangible property of all other commercial and industrial taxpayers is excluded from taxation. CSXT argues that the Department's valuation methods improperly compound intangible value, and CSXT urges the court to order the Department to use a yield capitalization approach, which CSXT claims will minimize the inclusion of intangible assets in the Department's valuation.

The matter was tried by the court sitting without a jury from May 16, 2005, through May 25, 2005. The court took the case under advisement pending the filing of post-trial briefs. The following order constitutes the court's findings of fact and conclusions of law as required by Federal Rule of Civil Procedure 52.

Factual Background

I. *The Parties*

A. *CSXT*

CSXT, the taxpayer in this case, is a Class 1 interstate common carrier by rail that operates in more than 71 counties in Georgia. It is subject to the jurisdiction of the Surface Transportation Board ("STB").

CSXT is a wholly-owned subsidiary of CSX Corporation. CSX Corporation's stock is publicly traded. As of January 1, 2002, CSX Corporation also owned several other subsidiaries including: (1) CSX World Terminals; (2) CSX Intermodal,

Inc.;[1] (3) CSX Lines; (4) CSX Technology, Inc.; and (5) CSX Hotels, Inc.

As of the fiscal year ending December 28, 2001, CSXT accounted for 75% of CSX Corporation's total operating revenues and 78% of its operating income.[2] CSXT's operating revenues for that year alone amounted to $6.082 billion with an adjusted operating income of $803 million.

By the mid-1990's only three Class 1 railroads existed and competed for freight traffic in the eastern half of the United States: (1) Consolidated Rail Corporation ("Conrail"), (2) Norfolk Southern Corporation ("Norfolk Southern"), and (3) CSXT. In August 1998, the STB approved the joint acquisition of Conrail by Norfolk Southern and CSX Corporation. The acquisition included an outright buyout of Conrail's assets by Norfolk Southern and CSX Corporation for approximately $10.5 billion and the assumption of net debt of $1.9 billion.

In June 1999, CSXT began operating portions of Conrail's system. By January 1, 2002, CSXT was operating approximately 42% of the former Conrail system. At that time, CSXT provided rail freight transportation over a network of approximately 40,000 miles of track and 23,000 route miles.[3] CSXT's network included a route through the southeastern United States, including Georgia, as well as a route from the New York/New Jersey area down the east coast to Florida.

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[1] CSX Intermodal ("CSXI") moves trailers or containers on flat cars to trucks. In addition, CSXI operates 33 terminals across the United States. When CSXI moves intermodal traffic over CSXT's system, CSXI pays CSXT a "transfer price" of approximately $350 to $400 million annually for CSXI's use of CSXT's resources and routes.

[2] Operating income is operating revenues minus total operating expenses.

[3] The acquisition of Conrail added 4,400 miles of track to CSXT's rail system in the Northeast United States and Canada.

CSXT's rail transportation property consists of a variety of items, including land, rail, track material, stations, and equipment. CSXT also operates rolling stock and equipment that it leases. During the time period in question, CSXT had between 34,000 and 36,000 employees and operated between 230,000 to 240,000 freight cars on its system.

Maintaining a rail transportation system requires heavy investment in capital expenditures.[4] Mr. Lewis, a Vice President of CSXT, testified that for the calendar years 2000 and 2001, CSXT's total capital expenditures were between $800 and $900 million.

The acquisition of Conrail had a noticeable effect on CSXT's revenues. For example, in 1997, CSXT's unlevered free cash flow was $467 million. In 1998, after the STB approved the Conrail merger, CSXT's unlevered free cash flow plummeted to negative $115 million. In 1999, CSXT' s [sic] unlevered free cash flow again plunged to negative $309 million. By 2000-2001, some efficiencies were beginning to be realized, and CSXT's unlevered free cash flow rose by 154.9% in two years.[5]

Similarly, the Conrail merger also had an effect on CSXT's operating ratio.[6] CSXT's operating ratio prior to the acquisition of Conrail was 75.4%. After acquiring Conrail, CSXT's operating ratio rose to a high of 89.9% and then began to decline again (to a more profitable ratio) in 2001.

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[4] The term "capital expenditure" refers to purchases of depreciable assets with long lives.

[5] In 2001 and 2002, CSXT Surface Transportation had a positive cash flow of around $150 million. Mr. Lewis testified that the positive cash flow was primarily due to real estate sales of $325 million.

[6] The term operating ratio refers to the ratio of operating expenses to revenue.

Although the acquisition of Conrail had a negative effect on CSXT's financial success in the short-run, the evidence at trial showed that it was likely that some efficiencies would be achieved in the future due to the merger. In fact, even CSXT's own expert, Mr. Tegarden, testified that some costs may be eliminated, which would increase future net operating income.

The evidence at trial also showed that railroads face considerable competition from other modes of transportation, such as trucks. Unlike trucks, however, railroads have to pay for and maintain their own infrastructure. Beginning in 1980, this competition steadily forced rates down. Taking trucks off the highways was the stated goal of the Conrail merger. To that end, the Conrail merger created a huge growth opportunity for CSXT. For instance, in 2001, CSXT was able to move 350,000 truckloads of merchandise off the roads and onto their rails.

B. *The Defendants*

The defendants are the Board and its individual members, including Bart L. Graham, the State Commissioner of Revenue.

The appraised and assessed values of most property in Georgia are determined by county boards of assessors. The parties refer to this property as "locally-assessed" property. Pursuant to O.C.G.A. § 48-5-6, most locally-assessed property subject to taxation in Georgia is to be appraised for assessment purposes at its fair market value. After any such nonexempt locally-assessed property in Georgia is appraised at its fair market value, an assessment ratio of 40% is applied to the appraised value to derive the assessed value. It is this assessed value against which property tax is levied and collected.

Companies classified in Georgia as "public utilities" are commonly referred to as "centrally-assessed" taxpayers. Centrally-assessed taxpayers include railroads, investor-owned electric utilities, investor-owned telephone companies, pipeline companies, and gas distribution companies. The State Revenue Commissioner issues proposed assessments of the operating and non-operating property of public utilities such as CSXT.

The Property Tax Division of the Department annually prepares a proposed assessment of CSXT's railroad transportation operating property for every Georgia county in which CSXT's taxable property is located.

II. *The Department's Proposed Valuation of CSXT*

In Georgia, the procedure for assessing rail transportation property is set forth in O.C.G.A. § 48-2-18. Under that statute, the Board approves an initial, proposed assessment of the taxpayer's property, and certifies that assessment to the counties in which the taxpayer owns taxable property. *Id.* § 48-2-18(c). *See also Telecom USA, Inc. v. Collins*, 260 Ga. 362, 364-65, 393 S.E.2d 235, 238 (1990) (discussing revised Georgia tax assessment procedures); *Colonial Pipeline Co. v. Collins*, 921 F.2d 1237 (11th Cir.1991) (same). Each county must then issue its final assessment to the taxpayer within 30 days; in doing so, "a county may, but is not required to, use the[ ] figures [provided by the Board] as the county's own tax assessment." *Colonial Pipeline*, 921 F.2d at 1240-41.

The Department used the unit rule method to value CSXT's railroad transportation operating property for 2002 ad valorem tax purposes. The unit rule method values the entire operating system of CSXT as a going concern and integrated whole irregardless of where it is located and without functional or geographic division of the whole into its component parts. A unit value determined pursuant to the unit rule method is meant to capture all of the operating assets

of the company whether owned or used. The parties agree that the unit rule method is appropriate under Georgia law.

Gregg Dickerson is the Program Manager in the Public Utilities Section of the Local Government Services Division of the Department. Mr. Dickerson first joined the Department in 1983 and spent ten years doing valuations pursuant to the unit rule method for centrally-assessed public utilities, including railroads. In 1993, he left the Department and went to work for Norfolk Southern railroad as a property tax manager, where his duties included reviewing and negotiating unit values with various states.

In the fall of 2001, Mr. Dickerson was approached by the then-director of the Department, Mr. Larry Griggers, who asked him to return to the Department. Mr. Griggers stated that he was concerned that the public utility digest for Georgia had decreased from 10% to 5% of the total state property tax digest since Mr. Dickerson's departure. Mr. Dickerson agreed to return, but stated that he would not come back for the purpose of "raising the numbers." He would only come back if Mr. Griggers' purpose was to "get[ ] the numbers right." Mr. Griggers agreed and Mr. Dickerson returned to work for the Department in September 2001. Mr. Dickerson was the individual responsible for preparing the valuation worksheets that served as the basis for the Department's Proposed Valuation of CSXT for the tax year 2002.

Applying the unit rule method, Mr. Dickerson first prepared a Railroad Valuation Worksheet. The Railroad Valuation Worksheet calculated CSXT's unit value using three valuation methods: (1) a stock and debt approach, (2) a discounted cash flow ("DCF") approach, and (3) a market

multiple approach. These different approaches yielded the following values:

Stock and Debt	$12.022 billion
DCF	$8.126 billion
Market Multiples[7]	$12.346 billion
	$10.769 billion
	$8.474 billion

After coming up with this range of values for CSXT, Mr. Dickerson selected $8.2 billion as the lower limit of what the going concern unit value of CSXT could reasonably be. He then used $8.2 billion as the foundation for the Department's Proposed Valuation.

After determining the unit value for CSXT, Mr. Dickerson then estimated a working capital adjustment of $400 million and deducted that from his unit value estimate of $8.2 billion to eliminate the effect of certain intangible assets. Next, Mr. Dickerson allocated the adjusted unit value estimate of $7.8 billion to the state of Georgia by using the percentage of Georgia road miles to system road miles. For the tax year 2002, the percentage so applied equaled 7.194059%, resulting in an allocated value of $561,136,602 for the state of Georgia.

To arrive at CSXT's proposed taxable fair market value in Georgia, Mr. Dickerson then deducted amounts for motor vehicles, exempt pollution control equipment, and exempt railroad lines. As a result, Mr. Dickerson determined that CSXT's taxable fair market value in Georgia for the tax year 2002 was $514,862,671 and presented this number to the Board.

Following the Board's approval, the Department issued a Notice of Proposed Assessment dated November 25, 2002

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[7] The market multiple approach yielded three different values because the Department calculated three different "multiples."

(the "Proposed Assessment"), to CSXT and to the counties in which CSXT had taxable property. The Proposed Assessment included three components: (1) the portion of the Department's proposed taxable fair market value of CSXT's operating property in Georgia attributable to each county, (2) the level of assessment that the Board determined each county should use, and (3) a proposed assessment for each Georgia county in which CSXT had taxable property, which was derived by multiplying the county's distributed value by 40% or the prevailing level of assessment in that county.

After this litigation commenced, in November 2003, Mr. Dickerson prepared a complete appraisal of CSXT using essentially the same three valuation methods that he employed with the Proposed Valuation. The purpose of this appraisal was to provide the court with Mr. Dickerson's point estimate of CSXT's unit value, rather than a figure at the lower end of his range of fair market values.

Following the close of fact discovery in this case, Mr. Dickerson prepared a revised full appraisal of CSXT in support of the Proposed Valuation. The only difference between Mr. Dickerson's November 2003 appraisal and the revised appraisal involved a change in the calculation of the cost of equity used in deriving the weighted cost of capital. The range of values Mr. Dickerson arrived at in his second appraisal were:

Stock and Debt	$12.128 billion
DCF	$10.960 billion
Market Multiples	$12.434 billion
	$10.871 billion
	$8.986 billion

Based on this range of values, Mr. Dickerson opined that the fair market system value of CSXT as of January 1, 2002, prior to adjustments for leases was $11 billion. Mr. Dic-

kerson then added $807 million to this value to account for the value of CSXT's operating leases. He ultimately opined that the fair market unit value of CSXT was $11.807 billion.

III. *An Overview of the Parties' Valuation Approaches*

As noted above, in Georgia, as in most states, a railroad's operating property is valued for property tax purposes as a unit. Under the unit concept of value, the fair market value of the railroad is measured by appraising the whole property as a going concern. To determine the unit value of a company, the appraiser must first choose from and apply a variety of valuation methods.

There are three general approaches to valuing a company or property: (1) the sales comparison approach, (2) the income approach, and (3) the cost approach. The standard sales comparison approach determines the value of a property or company by examining and comparing actual sales of comparable properties or companies. Conversely, the cost approach determines the value of a property by totaling the original costs of the various components of the property, and then making adjustments to account for depreciation or obsolescence. The theory behind the income approach is that anyone who buys a company buys it only for the income the company will generate.

Mr. Dickerson's responsibilities in preparing proposed assessments for centrally-assessed property for the tax year 2002 included reviewing the valuation methods that had been used by the Department in the past. As a result of his analysis, Mr. Dickerson made certain changes to the valuation methods used for all centrally-assessed taxpayers subject to the unit rule method. Those changes, which were applied on an across-the-board basis, included replacing the existing capitalized earnings approach with a DCF model. He also

replaced what had been labeled as a direct capitalization approach with a market multiple approach.

For CSXT, Mr. Dickerson used three different valuation methods: (1) a stock and debt approach, (2) a DCF approach, and (3) a market multiple approach. In rough terms, the stock and debt method is a surrogate for the sales comparison approach. It assumes that the value of a company equals all of the outstanding debt owned by that company plus the company's equity. Similarly, the market multiple approach is also a substitute for the sales comparison approach. Under a market multiple approach, the appraiser derives market multiples from the stock prices of companies that are engaged in similar lines of business and compares those multiples with the subject company to determine the value of that company.

Unlike the stock and debt and market multiple approaches, the DCF approach is a version of the income approach. Under the DCF approach, the appraiser makes assumptions to project cash flows for the company for a designated number of years after the assessment date, and then discounts those expected cash flows to their present value. The appraiser then calculates a terminal or reversion value representing the value of the company at the end of the projection period. The total of the discounted cash flows during the projection period and the terminal value gives the appraiser his unit value for the company.

CSXT's valuation expert, Mr. Tegarden, also used three valuation methods to value CSXT: (1) a stock and debt approach, (2) a cost approach, and (3) a yield capitalization approach. The yield capitalization approach is another variation of the income approach. It can perhaps be described

as a cousin of the Department's DCF approach. For example, the Department's DCF model is expressed as:

$$V = \frac{(CF1)}{(1+k)} + \ldots \frac{(CFn)}{(1+k)} + \frac{T}{(1+k)}$$

Cfn = net cash flow for the year n, k = discount rate, T = terminal value, and n = year. Mr. Tegarden's yield capitalization approach is expressed by the formula:

$$V = \frac{I}{r}$$

I = income and r = discount rate.

Mr. Tegarden gave no weight to his stock and debt value, very little weight to his calculations under the cost approach, and primary weight to his yield capitalization value. Using this weighted scale, Mr. Tegarden picked approximately $6 billion as the unit value of CSXT.

Legal Analysis

I. *The 4-R Act*

The 4-R Act prohibits a state from "[a] ssess[ing] [sic] rail transportation property at a value that has a higher ratio to [its] true market value . . . than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to [its] true market value. . . ." 49 U.S.C. § 11501(b)(1). The 4-R Act also prohibits states from levying or collecting taxes based on such an assessment, or otherwise discriminating against rail carriers in taxation. *Id.* § 11501(b)(2)-(4). "Assessment" is defined in the 4-R Act as "valuation for a property tax levied by a taxing district." *Id.* § 11501(a)(1).

II. *Burden of Proof*

The burden of proof in a case brought under the 4-R Act is determined by state law. 49 U.S.C. § 11501(c). The 4-R Act

requires a district court to use the burden of proof generally applicable to civil proceedings. *See Burlington Northern Railroad Co. v. Bair*, 766 F.2d 1222, 1226 (8th Cir.1985); *Atchison, Topeka, and Santa Fe Railway v. Lennen*, 732 F.2d 1495, 1500 (10th Cir.1984). In Georgia, a preponderance of the evidence is "the essential quantum of evidence . . . necessary to satisfy the minds of the fact finders in civil cases." *Ocean Accident & Guarantee Corp. v. Bates*, 104 Ga.App. 621, 622, 122 S.E.2d 305, 307 (1961). Thus, CSXT' s [sic] burden is the preponderance of the evidence standard.[8]

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[8] The defendants contend that the court must accept their tax assessment as prima facie correct, and that the burden is on CSXT to show that their assessment is in error. The defendants' argument is based on their belief that the burden of proof applicable in this case is the same burden of proof used when a taxpayer litigates the assessment they received in Georgia. This is not, however, a case where CSXT is simply appealing the Department's assessment. This is a case brought under the 4-R Act and the court must determine the true market value of CSXT. CSXT, in turn, has the burden of proving by a preponderance of the evidence that the true market value of its property is $6 billion. To do this, CSXT presented two types of evidence. First, it criticized the Department's calculations. Second, it presented a valuation of its property by Mr. Tegarden. In a more typical case, the court would look at both Mr. Tegarden's appraisal and the Department's appraisal to determine the true market value of CSXT. If the court found by a preponderance of the evidence that CSXT's true market value was $6 billion, as proposed by CSXT, then the court would compare the Department's Proposed Valuation to CSXT's true market value to determine if discrimination occurred. However, as explained later in this order, the court cannot consider Mr. Tegarden's valuation because it was prepared using different valuation methods than the Department. The court, therefore, is limited to looking solely at CSXT's criticisms of the Department's valuation.

III. *Whether the Department Assessed CSXT's Operating Property in Georgia for the Tax Year 2002 in Excess of its True Market Value, Resulting in a Ratio of Assessed Value to True Market Value for CSXT's Property which Exceeds by More than 5% the Ratio of Assessed Value to True Market Value of Other Commercial and Industrial Property in Georgia*

A. *May CSXT Challenge the Department's Chosen Valuation Methods?*

In this case, the parties disagree over the proper way to calculate the value of CSXT under each valuation method. Significantly, the parties also disagree over which valuation method the Department should use to value CSXT.

One of the problems with subjecting complex issues like valuation to judicial determination is that the court generally must choose among the competing claims of experts. Unless the court performs its own appraisal, the court must rely either on CSXT's experts or the Department's experts. The court, of course, may adjust an expert's appraisal up or down based on other experts' critiques of the appraisal, but the starting point for judicial determination is always one appraisal or another, and each appraisal is based on a particular methodology that, to a large extent, predetermines the result. Thus, implicit in the court's holding is a decision as to the proper valuation method.

The evidence shows that all five approaches used by CSXT and the Department, the yield capitalization, DCF, stock and debt, market multiple, and cost approaches, are widely used to value property. The question, then, is whether the Department is free to choose among accepted valuation methods or whether the 4-R Act compels the use of one particular method.

The United States Supreme Court in *Burlington Northern Railroad Co. v. Oklahoma Tax Commission*, 481 U.S. 454,

463 n. 5, 107 S.Ct. 1855, 1861 n. 5, 95 L.Ed.2d 404 (1987), expressly left open the question of "whether a railroad may, in an action under [the 4-R Act], challenge the appropriateness of the accounting methods by which the state has determined the railroad's value, or is instead restricted to challenging the factual determinations to which the state's preferred accounting methods were applied." *Id.*

Since the *Burlington Northern* decision, several courts have answered this question. Perhaps the most followed decision is the Fourth Circuit's decision in *Chesapeake Western Railway v. Forst*, 938 F.2d 528, 533 (4th Cir.1991), *cert. denied*, 503 U.S. 966, 112 S.Ct. 1577, 118 L.Ed.2d 220 (1992). *See also Burlington Northern Railroad Co. v. Bair*, 815 F.Supp. 1223, 1228-29 (S.D.Iowa 1993) (following *Chesapeake* and holding that a railroad may not challenge the state's chosen methodology); *cf. Union Pacific Railroad Co. v. State Tax Commission of Utah*, 716 F.Supp. 543, 556-57 (D.Utah 1988) (holding that as long as the state's method has a rational basis and was not chosen for a discriminatory purpose, the court will not disturb the state's choice). In *Chesapeake*, the railroad brought an action challenging Virginia's "over the fence" method of valuing railroad property and arguing for use of the unit method. *Chesapeake*, 938 F.2d at 530. Relying primarily on the 4-R Act's legislative history, the Fourth Circuit concluded that the 4-R Act "does not provide a basis for railroads to challenge a state's preferred methodology for ascertaining the true market value of railroad property." *Id.* at 533; *see also Richmond, Fredericksburg & Potomac Co. v. Forst*, 4 F.3d 244, 250 (4th Cir.1993) ("[A] railroad may present independent evidence of the fair market value of its property, provided, of course, that it limits its evidence to factors that may properly be taken into account under the state's chosen methodology.").

As support for its argument that the court should allow it to challenge the Department's valuation methods, CSXT cites to

decisions from the Second and Ninth Circuit. Neither of these circuits, however, allowed a railroad to freely challenge the state's methodology. For instance, in *Consolidated Rail Corp. v. Town of Hyde Park*, 47 F.3d 473, 482 (2d Cir.1995), the Second Circuit held that the state must apply the "same valuation standard and methods to the railroad property as are used on the commercial and industrial properties to which [the railroad] is compared." The implicit holding in *Hyde Park*, therefore, is that a railroad cannot challenge the state's valuation methods as long as the state uses the same methods for other commercial taxpayers. Here, the evidence at trial showed that the Department used essentially the same valuation methods for CSXT that it used for other centrally-assessed taxpayers.

Similarly, while the Ninth Circuit allowed a railroad to challenge the state's chosen methodology, it also held that the state's chosen methodology is presumed correct and can be defeated only by clear, cogent, and convincing evidence. *Burlington Northern Railroad v. Department of Revenue of the State of Washington*, 23 F.3d 239, 241 (9th Cir.1994).

Although the Eleventh Circuit has yet to address this question, the court finds that the legislative history, which is admittedly rather thin, supports the Fourth Circuit's determination that the 4-R Act does not confer jurisdiction upon this court to order the Department to use a specific accounting method to determine the value of CSXT. The committee report on Senate Bill 927, one of several precursors to the 4-R Act, states that:

> [The bill] does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves. It merely provides a single standard against which all affected assessments must be measured in order to determine their relationship to each other. It is not a standard for determining value; it is a

> standard to which values that have already been determined must be compared.

S.Rep. No. 1483, 90th Cong., 2d Sess.App. B (1968).

Similarly, in hearings on House Bill 16245, another forerunner of the 4-R Act, Mr. Lanier, a railroad representative, testified that, "[t]he standards and methods of valuation that any state wishes to use would be totally unaffected by this legislation." *Chesapeake*, 938 F.2d at 531 (*citing* Hearing Before the Subcommittee on Interstate and Foreign Commerce on H.R. 16245, 91st Cong., 1st Sess. 138 (1970)). Thus, the legislative history suggests that the statute was not meant to require a state to use a particular accounting method, at least as long as the state's chosen methods are rational and were not chosen for a discriminatory purpose.

After eight days of trial, it is apparent to the court that valuation is an art, not a science. Valuing a business requires an appraiser to make "judgment calls," even under CSXT's yield capitalization method. Absent a willing buyer and a willing seller, the determination of true market value for purposes of ad valorem taxation is always an estimate, always an expression of judgment, and always a result built on "judgment calls." The appraisals in this case are good examples of this. Mr. Tegarden and Mr. Dickerson each used at least three different valuation methods to arrive at the market value of CSXT. Both Mr. Tegarden and Mr. Dickerson arrived at different conclusions as to the value of CSXT under each method that they utilized. For example, CSXT's own expert, Mr. Tegarden, arrived at the following three values for CSXT for the tax year 2002:

Cost Approach	$6.150 billion
Income Approach	$5.983 billion
Stock and Debt Approach	$9.637 billion

The $3 billion difference in Mr. Tegarden' s values makes clear that the determination of the true market value of CSXT in this case is, at best, an educated guess. The fact that the determination of CSXT's true market value is an educated guess weighs against the court requiring the Department to use a particular valuation method.

In addition to the fact that all appraisals are at best educated guesses, the court is unwilling to dictate a particular valuation method to the Department for other reasons. From the testimony of the Department's witnesses, the court concludes that the Department sincerely seeks to arrive at what it considers to be CSXT's true market value, and that, to that end, it constantly reevaluates its methods and changes them when the Department becomes convinced that they are erroneous. If this court were to conclude that the 4-R Act required the Department to adopt the yield capitalization method of valuation, it would prevent the Department from critically examining its appraisal methods and would discourage it from adopting new and better methods as they become accepted by the appraisal profession.

For all of these reasons, the court concludes that the 4-R Act does not generally allow a railroad to challenge the state's chosen methodology. As long as the Department's chosen valuation methods are rational and were not chosen for the purpose of discriminating against CSXT, the court will not second guess the Department's choice of methods.

Even if the court were forced to choose between competing valuation methods, the court finds that the Department's chosen methods have much to commend them. Not only does the Department consistently use essentially the same approach for all centrally-assessed property, but its valuation methods are based on historical and market data readily available to investors and to the defendants. All three of the Department's valuation methods are widely accepted and used by valuation experts. The fact that these methods are

widely used and accepted is evidenced not only by the testimony of the majority of experts, but also by the fact that they have been approved by other courts. *See, e.g., Bair*, 815 F.Supp. at 1228-29 (approving of the use of the stock and debt approach to valuing the BN railroad); *Burlington Northern Railroad Co. v. Department of Revenue of the State of Washington*, No. C90-5417, 1992 WL 201947, at *4-5 (W.D.Wash. Aug.13, 1992), *aff'd* 23 F.3d 239 (9th Cir.1994) (giving deference to the state's use of the stock and debt, DCF, and cost approaches).

(1) *Whether the Department's Chosen Valuation Methods Are Irrational*

The court finds that the Department's chosen valuation methods are rational. As noted above, the stock and debt approach, market multiple approach, and DCF approach have much to commend them. They are widely accepted and generally based on historic and market data readily available to the public and investors.

CSXT' s [sic] primary criticism of the Department's valuation methods is that they compound intangible values at a higher rate than CSXT's yield capitalization method does. For example, CSXT introduced testimony showing that stock prices include value attributable to intangible property. Because all three of the Department's valuation methods utilize stock prices derived from CSX Corporation, CSXT's parent company, CSXT argues that the Department's approaches are flawed.

The court agrees that stock prices include intangible value, whether it is "intangible influences" or "intangible property." By extension, therefore, any approach that utilizes stock prices includes some intangible value. Nevertheless, the fact that the Department's approaches include intangible value does not make their use irrational. Both parties' experts agree that the fair market value of a business is meant to

value what a willing buyer would pay for that business. Stock prices, thus, are particularly relevant for appraisal purposes because absent a recent sale of the business, the company's stock price is the only real example of what a willing buyer would pay for a share of that business.

The court also points out that CSXT's own valuation methods are not exempt from the same criticism. It is undisputed that CSXT's yield capitalization method relies to some extent on stock prices and includes at least some value attributable to intangible property.

(2) *Whether the Department's Chosen Valuation Methods Were Adopted for a Discriminatory Purpose*

The court also finds that the evidence at trial does not support the conclusion that the Department selected the DCF approach, the stock and debt approach, or the market multiple approach for the purpose of discriminating against CSXT. The evidence at trial showed that the Department utilizes essentially these same methods when valuing non-railroad centrally-assessed property.

Accordingly, the court concludes that CSXT cannot challenge the Department's chosen valuation methods in this case. This ruling, of course, does not prevent CSXT from challenging the manner in which the Department calculated the value of CSXT using its stock and debt, DCF, and market multiple approaches.

B. *Can the Court Consider Mr. Tegarden's Appraisal of CSXT?*

The court is required to weigh the evidence and make its own factual findings regarding the true market value of CSXT. The question then arises as to whether the court can consider evidence of the true market value of CSXT' s [sic] operating property determined by a valuation method not employed by the Department. The court finds that it cannot

do so in this case because the valuation methods chosen by the Department are rational and were not adopted for a discriminatory purpose.

The court must make its factual findings as to the value of CSXT using the methods utilized by the Department. Otherwise, the court will be, in effect, ordering the Department to use a different valuation method.

It is undisputed that the Department used a DCF approach, a stock and debt approach, and a market multiple approach to value CSXT. CSXT's expert, Mr. Tegarden, appraised CSXT using a yield capitalization approach, a stock and debt approach, and a cost approach. Mr. Tegarden testified that he placed no weight on his calculations under the stock and debt approach and little emphasis on his calculations under the cost approach. Therefore, the court concludes that Mr. Tegarden's appraisal is based primarily on the yield capitalization approach with some small emphasis on the cost approach.[9]

The court concludes that both the cost approach and the yield capitalization approach are different valuation methods than the Department's valuation methods. Although the yield capitalization approach is undoubtedly a cousin of the Department's DCF approach, the fact that it is truly a different valuation method is most aptly illustrated by the fact that CSXT spent much of its time at trial arguing that the court should order the Department to adopt the yield capitalization approach because the other methods used by the Department to value CSXT were flawed.

Because the yield capitalization and cost approaches are different valuation methods than the methods used by the

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[9] CSXT admits that the cost approach is not particularly reliable for use in valuing railroad assets because of the substantial obsolescence affecting railroad property. Pl.'s Post-Trial Br. at 22 [Doc. No. 113].

Department, the court cannot consider Mr. Tegarden's valuation of CSXT under these approaches. Since CSXT has introduced into evidence no other appraisal of its property using the valuation methods employed by the Department, the court must necessarily limit its analysis to the criticisms presented by CSXT as to the manner in which the Department calculated the value of CSXT under its DCF, stock and debt, and market multiple approaches.

C. *The Department's Appraisals*

Before the court reaches CSXT's criticisms of the Department's calculations, the court must first address the two appraisals created by the Department after the commencement of this litigation. As noted earlier, after this litigation commenced, the Department prepared two appraisals of CSXT. The purpose of these appraisals was to provide the court with Mr. Dickerson's point estimate of CSXT's unit value, rather than a figure at the lower end of his range of fair market values. The only difference between the two appraisals was a change in the calculation of the cost of equity used in deriving the weighted cost of capital.

The fact that the Department created two appraisals significantly complicates this case. The Department urges the court to disregard its original Proposed Valuation and hold that the actual fair market unit value of CSXT is $11.807 billion, which is the value derived from Mr. Dickerson' s [sic] revised appraisal. CSXT, however, focused the majority of its time at trial and in its post-trial briefs challenging the Department's Proposed Valuation.

The court has considered the Department's revised appraisal. As noted earlier, in its revised appraisal, the Department changed the way it calculated the cost of equity used in deriving the weighted cost of capital for CSXT. It appears to the court that the Department created this new method of calculating the cost of equity in late 2003 or early 2004 and,

thus, did not apply this formula to any other taxpayer in 2002. The court questions the relevancy of the revised appraisal for use in this lawsuit. The methods used were not applied to other taxpayers for the year 2002, and the revised appraisal was not used by the Department in assessing the values at issue here. The controversy before the court is the methods and the amounts used, not what could have been used. The court's analysis and approval (or disapproval) of the revised appraisal essentially amounts to an "advisory" opinion. Further, applying this new method of calculating the cost of equity to CSXT when it was not used for any other taxpayer would be inherently discriminatory. Accordingly, the court will focus the remainder of this order on the Department's Proposed Valuation.

D. *CSXT's Criticisms of the Department's Calculations*

As noted above, the Department utilized three methods for determining the fair market value of CSXT: (1) the stock and debt approach, (2) the DCF approach, and (3) the market multiple approach. Each of these approaches yielded a different unit value for CSXT. From this range of values, Mr. Dickerson then chose a number, $8.2 billion, that was closest to the lowest value in that range. The $8.2 billion unit value became the foundation for the Department's Proposed Valuation.

CSXT challenges the calculations made by Mr. Dickerson under his Proposed Valuation on four grounds. First, CSXT claims that the Department made errors in its DCF analysis. Second, CSXT claims that the Department calculated excessive stock and debt figures. Third, CSXT claims that the Department utilized excessive market multiple figures. Finally, CSXT claims that the Department improperly double-counted the value of CSXT's leased equipment.

(1) *CSXT's Criticisms of the Department's DCF Analysis*

To arrive at the DCF value of CSXT, the Department first calculated CSXT's anticipated future operating free cash flows for a ten-year period from 2002 to 2011 based on projections regarding the growth rate of CSXT's revenues, expenses, and capital expenditures. The Department then calculated a terminal value for CSXT (i.e., what a purchaser would expect to pay for the company at the end of the period). Next, the Department discounted this cash flow to January 1, 2002, using as the discount rate a 9.90% after-tax average weighted cost of capital. This calculation yielded a figure of $7,518,317,142, to which the Department added an amount for leased equipment of $607,976,209 to come up with a DCF value of CSXT of $8,126,293,350.

In particular, the Department's DCF model projected an increase in CSXT's cash flow of 69% from 2001 to 2002. The Department's model also projected a declining growth rate in cash flows from 5.32% in 2003 to 3.58% in 2011 and then assumed a constant terminal growth rate of 6.3% from 2011 into perpetuity. In addition, the Department assumed a 2% growth in revenues per year and projected that CSXT could achieve an 80% operating ratio by 2011.

According to CSXT, several of the assumptions in the Department's DCF model are erroneous because they allegedly have no basis in the historic record of CSXT's performance. In particular, CSXT claims that the Department erroneously projects: (1) a 69% increase in cash flow from 2001 to 2002, (2) a 6.3% terminal growth rate, and (3) an operating ratio of 80% by 2011. CSXT argues that these allegedly erroneous financial projections cause the Department's DCF model to overstate the value of CSXT.

(a) *The Department's Selection of 69% as the First Year's Cash Flow*

As noted above, the first year of the Department's DCF model assumes that CSXT's cash flow will increase by 69% over CSXT's actual cash flow for 2001. CSXT argues that this increase is bizarre and unsupported by the record. CSXT, however, introduced no evidence at trial as to what increase, if any, the Department should have projected or how that change would have affected the Department's value. In fact, instead of presenting testimony as to what the percentage increase or decrease the Department should have used and how changing that number affects the Department's DCF value for CSXT, CSXT argued that the court should correct the Department's projected terminal growth rate.

Regardless, the court finds that a 69% increase in projected cash flow from 2001 to 2002 is not bizarre. The evidence at trial showed that CSXT' s [sic] cash flow from 1991-2001 increased annually from 5.6% to 154.9% and sometimes declined. In fact, from 2000 to 2001, CSXT's unlevered free cash flow increased by more than 100%. Furthermore, as noted by CSXT' s [sic] expert at trial,[10] it is likely that some efficiencies may be achieved in the future due to the integration of CSXT and Conrail. These efficiencies will likely increase cash flow and reduce costs.

(b) *The Department's Selection of 6.3% as the Terminal Growth Rate*

CSXT next argues that the Department's decision to choose 6.3% as the terminal growth rate is excessively optimistic. CSXT points out that 6.3% is much higher than the growth rate that the Department projected for the years 2003-2011.

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[10] This statement was made by Mr. Tegarden in the context of explaining how he came up with $700 million as his estimate of CSXT's future net operating income.

CSXT also argues that the logical incongruence of the Department's terminal growth rate is indicated by the fact that the Department estimated that CSXT' s [sic] revenue would grow at only 2%. CSXT points out that if revenue grows at only 2%, while free cash flow (roughly revenue minus expenses) grows at 6.3% then at some point in time expenses would have to decline and become negative to sustain the 6.3% growth in free cash flow.

The court finds that the Department's decision to adopt a 6.3% terminal growth rate is not erroneous. First, to the extent that CSXT's experts opined that 6.3% was an unrealistic terminal growth rate, the court finds that their testimony was not credible. Second, the court notes that none of CSXT's experts testified as to what a proper terminal growth rate should be. At most, these experts suggested that the Department should have adopted 3.5% or 4.5% as the terminal growth rate. These "suggested" rates also suffer from some of the same infirmities that the rate selected by the Department does. For example, if revenues grow at 2%,[11] but free cash flow grows at any number higher than 2% (e.g., 3.5% or 4.5%) then eventually costs will have to decrease to a negative number.

(c) *The Department's Projected Operating Ratio*

CSXT also criticizes the operating ratio forecasted in the Department's Proposed Valuation. CSXT points out that it did not achieve its planned operating income or ratio from June 1999-December 2002. CSXT also presented evidence from Mr. Lewis, CSXT's Vice President of Finance, that the

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[11] Because the growth rate for revenue slowed to .4% per year from 1996 to 2001, CSXT also argues that the Department's projected growth rate of 2% per year for revenue is unduly optimistic. The court disagrees. CSXT admits that a 2% annual growth in revenue is not inconsistent with national trends for railroads between 1991 and 2001.

business risks facing the railroad industry make it "difficult to imagine . . . hav[ing] a lower operating ratio."

While it is true that CSXT did not achieve its planned operating ratios from 1999-2002, this fact alone does not indicate that the target operating ratios predicted by the Department were erroneous. Among other things, the Department estimated that CSXT would achieve an operating ratio of 80% by the year 2011. Eighty percent is consistent with CSXT' s [sic] strategic plan, its presentations to bond rating agencies, and the average historic operating ratios achieved by railroads, including CSXT, from 1995-2001. In fact, in 1998, prior to CSXT's acquisition of Conrail, CSXT achieved a 78.6% operating ratio. By 2001, CSXT's operating ratios had begun to decrease from a high of 89.9% in 2000. CSXT's 2001 Annual Report noted this change in trend stating, "With revenues expected to go up this year, the railroad's operating ratio, i.e., total costs as a percentage of total revenues, should improve considerably." Thus, it was reasonable for the Department to project that CSXT would achieve an operating ratio of 80% by the year 2011.

(2) *CSXT's Criticisms of the Department's Stock and Debt Analysis*

The Department determined the stock and debt value of CSXT by taking normalized year-end price data from Standard & Poor's Stock Guide and information from CSX Corporation's 2001 Annual Report. The Department concluded that the total market value of CSX Corporation's stock, its long-term debt, and the excess of current liabilities over current assets as of January 1, 2002, was $15,219,745,138. The Department next performed several calculations to determine what portion of this total was properly attributable to CSXT. The ratios the Department calculated were: 74. 91%, 81. 89%, 77. 93%, and 75. 47%. The Department selected 75% as a conservative number within that range. The Department then multiplied

$15,219,745,138 by 75% to come up with the portion of CSX Corporation's debt and equity which was allocable to CSXT. After adding $607 million for leased equipment, the Department arrived at $12,022,785,209 as the stock and debt value of CSXT.

In CSXT' s [sic] post-trial brief, CSXT points out a host of problems with the stock and debt approach generally, as opposed to problems with the Department's calculation of CSXT's stock and debt value. For example, CSXT argues that there is a disconnect between stock and debt values and the value of the taxable assets being valued in this case. CSXT points out that a company's stock price inevitably includes intangible values and assets not in existence on the date of the assessment, whereas an appraiser is only supposed to value tangible operating assets that are in existence as of the date of the appraisal.

As the court has previously indicated, it was proper for the Department to use the stock and debt approach to come up with a range of values for CSXT. *See Bair*, 815 F.Supp. at 1239 (approving of the use of the stock and debt approach in the appraisal of a railroad). The court, moreover, has already held that CSXT may not challenge the Department's chosen valuation methods.

In addition to criticisms of the stock and debt approach generally, CSXT argues that the stock and debt approach is not appropriate in this case because CSXT is not a publicly traded company. Although the stock of CSX Corporation is publicly traded and CSXT is wholly-owned by CSX Corporation, CSXT claims that it is difficult to identify a stock value attributable to CSXT' s [sic] railroad assets.

The court finds this argument unpersuasive. The mere fact that the Department must calculate and allocate a portion of CSX Corporation's stock to CSXT does not justify rejecting the Department's stock and debt value. Notably, CSXT does

not argue that the Department allocated the wrong proportion of CSX Corporation's equity to CSXT. In fact, it appears to the court that the parties agree that CSXT constitutes between 75-80% of CSX Corporation's total equity. CSXT's own expert, Mr. Tegarden, attributed 78.9% of CSX Corporation's total equity to CSXT when he calculated the discount rate in his yield capitalization approach.[12]

CSXT's final argument is that the Department erred by failing to make an adjustment to reflect the liquidity of stocks, as opposed to assets. CSXT points out that it is easier to buy a few units of stock, as opposed to the entire operating assets of a railroad. Because it is easier to buy stock, shares of stock reflect a liquidity premium that is not shared by the hard assets of a company.

Even if the court were to conclude that CSXT was correct, CSXT failed to present any expert testimony attesting as to how large an illiquidity discount the Department should have applied. At most, Mr. Tegarden' s [sic] report suggests that an illiquidity discount plus an adjustment for minority interests of 37.5% may be appropriate.[13] Pl.'s Ex. 1 at 60, n.

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[12] In other parts of its brief, CSXT suggests that the Department may have miscalculated the amount of debt attributable to CSXT. Even if the court were to accept this criticism, as well as CSXT's liquidity criticism described later in this opinion, according to the court's calculations the unit value of CSXT would be approximately $7.6 billion. This number is much higher than the $6 billion value proposed by CSXT.

Further, the court notes that the value of CSX Corporation's debt is $8.296 billion. If the court were to attribute 75% of CSX Corporation's debt to CSXT, the value of CSXT would be $6.2 billion. If, as CSXT claims, the value of CSXT was $6 billion, CSXT would have a negative equity value. CSX Corporation, however, held investment grade bond ratings implying a profitability level in excess of that needed to pay both current interest expenses and the principal balance of debt.

[13] If the court were to assume that CSXT's stock has a value in the market that is 37.5% higher than its underlying assets, according to the court's calculations the Department's stock and debt value of CSXT

46 ("Some studies have suggested that the effect of these two adjustments would be a reduction of the stock prices by approximately 37.5%."). This statement, however, is not specific to CSXT, nor does the court construe it as Mr. Tegarden's opinion regarding the actual illiquidity discount that should be applied to CSX Corporation's stock. In fact, Mr. Tegarden failed to include an illiquidity discount when arriving at his own stock and debt value.[14]

Nor is the court convinced that an illiquidity discount should be applied here. While stocks are undoubtedly more liquid than the entire operating assets of CSXT, buying the entire operating assets of a company gives the purchaser something that buying a few shares of stock cannot give him: control. One of CSXT's experts, Dr. Heaton, testified that an acquiring company will sometimes pay a control premium when the acquiring company believes that they can add value (create synergy) to the existing company. To the extent that any illiquidity discount may have been necessary, it may also have been completely offset by the necessity of adding a control premium.

(3) *CSXT's Criticisms of the Department's Market Multiple Analysis*

For the Department's market multiple approach, the Department identified six comparable railroads: (1) Burlington Northern, (2) Canadian National, (3) Canadian Pacific, (4) CSX Corporation, (5) Norfolk Southern, and (6) Union Pacific. The Department then multiplied the number of shares for these railroads by their year-end stock price to come up with the value of their equity. Next, the Department

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would be approximately $9.3 billion, much higher than Mr. Tegarden's $6 billion value for CSXT.

[14] In his appraisal report, Mr. Tegarden valued CSXT under the stock and debt approach at $9.637 billion. He testified that he gave little to no weight to this value because it did not include an illiquidity discount.

totaled the book value of the debt of these railroads, added the value of their equity, and subtracted cash items to derive each railroad's total market capitalization number. The Department then divided the total market capitalization number for each railroad by three different measures of income: revenues, EBIT,[15] and EBITDA.[16] This resulted in "multiples," which the Department applied against the same measures of income for CSXT to estimate the value of CSXT. The Department's market multiple values of CSXT were: (1) $12,246,460,000; (2) $10,769,011,960; and (3) $8,474,781,660 respectively.

CSXT primarily complains that the Department's calculation of its market multiple values is erroneous because the Department failed to make adjustments to its calculations to account for differences between these companies and CSXT. For example, CSXT argues that the Department failed to account for differences between the size of the comparator railroads and CSXT, whether they are eastern or western railroads, and the total amount of their assets. According to CSXT, if the Department had made the appropriate adjustments to reflect the differences between those railroads and CSXT, the appropriate market multiple value of CSXT would be approximately $6.08 billion.

Although the court applauds the Department's use of publicly traded Class 1[17] major railroads as comparable companies, the court finds that the Department erred when it failed to make adjustments to the size of the comparator companies. CSXT, however, has failed to introduce suf-

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[15] "EBIT" stands for "earnings before interest and tax."

[16] "EBITDA" stands for "earnings before interest, tax, and depreciation."

[17] As noted by Mr. Tegarden, the two Canadian railroads, Canadian National and Canadian Pacific, have enough revenue to be considered Class I railroads if they were U.S. companies.

ficient evidence for the court to determine what the appropriate adjustments should have been. At trial, CSXT introduced into evidence Plaintiff's Exhibit 51, which purports to adjust the values of Burlington Northern, Norfolk Southern, and Union Pacific to account for their size in comparison to CSXT. In addition to the fact that it does not make adjustments for all of the railroads used by the Department, it is not clear to the court whether the exhibit properly adjusts CSXT' s [sic] size to account for the purchase of Conrail. Nevertheless, because the Department erred in calculating its market multiple approach, the court will disregard the values the Department arrived at under its market multiple approach.

(4) *CSXT's Criticisms of the Department's Add-Back to Account for CSXT's Leased Equipment*

CSXT, like most railroads, leases substantial numbers of "rolling stock," such as locomotives and freight cars. The Conrail transaction was also structured using leases. CSXT uses operating leases to pay for various Conrail road assets. To account for this leased equipment and the Conrail road assets, the Department added $607 million to the unit value of CSXT under each of its valuation methods.

According to CSXT, the addition of $607 million to account for CSXT's leased assets is unnecessary because the Department's unit value of CSXT under all three valuation methods includes the value of all operating property owned or used by CSXT, including its leased assets. CSXT also argues that if the Department was going to treat CSXT's leased assets as if they were owned, the Department should have recognized that CSXT's capital expenditures would have increased if CSXT purchased its leased assets. If capital expenditures increased, then CSXT's cash flow would have been lower. The failure to make this adjustment to capital expenditures results in double counting the value of the leased assets.

In response, the Department points out that CSXT's operating leases are off-balance sheet financing. Because the operating leases do not show up on CSXT's balance sheet, the full value of the operating leases are not captured in CSXT's stock and debt prices or in the Department's income approach, unless certain adjustments are made.

After much deliberation, the court concludes that the Department did not improperly double count CSXT's leased assets. In particular, the court finds Dr. Ifflander and Mr. Dickerson's testimony on this issue credible.

There are two types of leases: capital leases and operating leases. A capital lease generally lasts for the life of an asset and the lease can be renewed at the end of the asset's life or the asset may be acquired at a favorable price. An operating lease usually lasts for a period of time much shorter than the actual life of the asset, and the present value of lease payments is generally much lower than the actual price of the asset. At the end of the life of the operating lease, the equipment usually reverts back to the lessor.

Under standard accounting rules, a capital lease is treated like a purchase. It shows up on a company's books as an asset, and the lease obligations show up as a liability or debt. Operating leases, on the other hand, do not show up on a company's books as an asset or a debt—they are off-balance sheet.[18] Instead, payments for operating leases show up as cash outflows from operations.[19]

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[18] The term "off-balance sheet" debt has been the focus of much attention in the last few years due to the Enron scandal. One of the principal ways in which Enron was able to deceive investors as to its value was by engaging in extensive off-balance sheet financing transactions, which shifted debt off Enron's balance sheet, making the company's balance sheet look far stronger than it actually was. *See* Lawrence E. Mitchell, *The Sarbanes-Oxley Act and the Reinvention of Corporate Governance?* Vill. L.Rev. 1189, 1212 (2003).

[19] "Off-balance sheet financing has been used for many years as a source of capital financing for acquiring heavy equipment, especially

When a lease arrangement is treated as off-balance sheet financing, the court is satisfied that there are "real current or future cash flow consequences." *See* 1 D.R. Carmichael & Paul Rosenfield, ACCOUNTANTS' HANDBOOK 33 (10th ed.2003). There are also consequences for reported earnings, book value of debt and capital, and return ratios for the company. The court finds that operating[20] and net income are lower, debt and capital for the firm are understated, and return on equity and capital are much higher. Unless an adjustment is made to the income statements to treat CSXT's leased Conrail road assets as if they were owned, the estimated market value CSXT will be understated.[21] In this case, the Department properly made such an adjustment—$607 million

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aircraft. . . ." John C. Murray, *Recharacterization and Title Issues in Synthetic Leasing Transactions*, 479 Practicing L. Inst./Real Est. Handbook 889 (2000).

[20] Operating income is a key input in both parties' valuation methods, but especially the DCF method.

[21] The court is aware of the fact that the Southern District of Iowa in *Burlington Northern Railroad Co. v. Bair*, 815 F.Supp. 1223, 1231 (S.D. Iowa 1993), reached a seemingly different conclusion. Although the *Bair* decision is not binding upon this court, the court points out that the *Bair* court's analysis on this issue is rather perfunctory. Further, in *Bair*, the court appears to have held that because commercial and industrial personal property is exempt from taxation, adding it back to the state's unit value estimations improperly double-counts the value of the leased rolling stock. *Id.* at 1231. In Georgia, however, taxable property is defined as "all real property, including but not limited to leaseholds, interests less than fee, and all personal property. . . ." O.C.G.A. § 48-5-3. Furthermore, Georgia law also states that a railroad's rolling stock and other personal property appurtenant to the rolling stock shall be taxed on "as much as the whole value of the rolling stock and personal property as the length of the railroad in this state bears to the whole length of the railroad, without regard to the location of the head office of the railroad. . . ." O.C.G.A. § 48-5-520. Thus, there does not appear to be a comparable tax exemption in Georgia.

to the unit value of CSXT under each of the Department's valuation methods.[22]

E. *The Court's Conclusions Regarding the True Market Value of CSXT*

After parsing through days of expert testimony, the court concludes that the Department's DCF value as set out in its Proposed Valuation is the most accurate indicator of CSXT's unit value. As a result, the court holds that, for purposes of applying the 4-R Act to the defendants' assessments of CSXT, the true market unit value of CSXT for the tax year 2002 was $7,726,293,350.[23]

The court finds that the portion of CSXT's true market value that should be allocated to Georgia for the tax year 2002 is 7.194059%. The true market value of CSXT's taxable rail transportation property in Georgia for the tax year 2002, therefore, was $509,560,171.[24]

Determining the true market value of CSXT does not end the inquiry. CSXT is only entitled to relief if the "ratio of [its] assessed value to [its] true market value . . . exceeds by at least 5% the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." 49 U.S.C. § 11501(c). The parties have stipulated that the ratio of assessed value to true market

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[22] Except for arguing that no adjustment is necessary, CSXT has offered no evidence as to what the amount of the adjustment should have been.

[23] The court arrived at this number by taking the Department's $8,126,293,350 DCF value for CSXT and subtracting $400 million to account for CSXT's intangible property.

[24] The court reached this number by taking the $7,726,293,350 true market unit value of CSXT and allocating 7.194059% to Georgia. The court then deducted $4,156,193 to account for CSXT's motor vehicles, $2,907,467 to account for pollution control, and $39,210,271 to account for W & A exempt line.

value for all other commercial and industrial property in Georgia is 40%. For CSXT to succeed against the defendants, therefore, the ratio of assessed value to true market value of CSXT's rail transportation property in each assessment jurisdiction must be at least 42%.[25]

Regardless of whether the assessment jurisdiction is the county or the state, the ratio of assessed market value to true market value for CSXT's rail transportation property is less than 42%. As a result, the court concludes that the defendants have not discriminated against CSXT in violation of 49 U.S.C. § 11501(b)(1).

IV. *Whether the Defendants Singled Out CSXT for Discriminatory Treatment by Applying a Higher Valuation Approach to CSXT's Property than the Valuation Approach Applied to Other Centrally-Assessed Taxpayers in Georgia for the Tax Year 2002 in Violation of 49 U.S.C. § 11501(b)(4)*

The provisions of 49 U.S.C. § 11501(b)(4) forbid the imposition of any tax that discriminates against a railroad. The United States Supreme Court has held that when railroads are singled out for discriminatory treatment, discrimination under 49 U.S.C. § 11501(b)(4) has occurred. *See Department of Revenue of Oregon v. ACF Industries, Inc.*, 510 U.S. 332, 346-47, 114 S.Ct. 843, 851, 127 L.Ed.2d 165 (1994).

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[25] Section 11501(c) states that relief may be granted under this section "only if the ratio of assessed value to true market value of rail transportation property exceeds by at least 5% the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." Once the 5% threshold is satisfied, the court is empowered to prevent all discrimination against the railroad. The 5% threshold is calculated by measuring 5% of 40%, which yields two percentage points. *See Southern Railway Co. v. State Board of Equalization*, 712 F.Supp. 1557, 1565-66 (N.D.Ga.1988).

CSXT claims that it has been singled out for discriminatory treatment because the Department did not attempt to assess the fair market value of other centrally-assessed taxpayers. Instead, CSXT claims that other centrally-assessed taxpayers are being taxed at whatever the Department determines is the lowest estimate of value that it could reasonably accept. CSXT argues that it is entitled to taxation on the same basis as these other centrally-assessed utilities-taxation based on the lowest possible value.

CSXT also argues that it has been treated differently than Norfolk Southern, the only other major railroad in Georgia. As evidence of this discrimination, CSXT points out that the Department consistently valued Norfolk Southern higher than CSXT, yet in the course of other litigation, the Department agreed to value Norfolk Southern at less than $8.2 billion for the tax year 2002.

A. *Whether CSXT Has Been Taxed Differently Than Other Centrally-Assessed Taxpayers*

CSXT first claims it has been singled out for discriminatory treatment because the Department's assessments of non-railroad centrally-assessed taxpayers are not based on the appraiser's opinion of the fair market value of those properties. In support of this claim, CSXT points out that Mr. Dickerson testified that he prepared proposed assessments for non-railroad utilities that represented the "lowest number he could come up with" and a "number at the lower end of his range of fair market value." Presumably because CSXT can come up with a lower number for its value than the Department, CSXT argues that it was treated differently than other centrally-assessed taxpayers.

The court finds CSXT' s [sic] argument unpersuasive. The evidence at trial showed that in preparing the Department's proposed valuations of CSXT and other taxpayers subject to the unit rule method, Mr. Dickerson first determined the

range within which he thought a particular company's fair market value could lie and then chose a number at the lower end of this range. CSXT was treated in the same manner as other public utilities; Mr. Dickerson came up with a range of values for CSXT and then picked a number that was closest to the lower end of that range. Further, the evidence at trial showed that Mr. Dickerson used essentially the same valuation methods to determine the unit value of all taxpayers subject to the unit rule method. The court finds Mr. Dickerson' s [sic] testimony on this issue to be credible.

Moreover, the fact that CSXT could come up with a lower number than the Department is meaningless. The Department did not base its valuation of other centrally-assessed taxpayers on the lowest number those taxpayers could come up with.[26] Instead, centrally-assessed taxpayers were taxed at the lowest number that Mr. Dickerson could come up with, just as CSXT was.

As further evidence that CSXT has been singled out for discriminatory treatment, CSXT argues that the Department's Proposed Valuation for 2002 is 47.1% higher than CSXT's 2001 assessment, whereas other non-railroad centrally-assessed taxpayers suffered only minimal increases. According to CSXT, this large increase was primarily caused by the exceedingly high terminal growth rate that Mr. Dickerson used in his DCF approach.

The fact that CSXT' s [sic] 2002 assessment was 47.1% higher than its 2001 assessment, and that this percentage increase is much higher than the percentage increase of other centrally-assessed taxpayers, does not in and of itself show that CSXT has been discriminated against. An equally likely proposition is that CSXT was undervalued in 2001. Further,

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[26] The court has no doubt that other centrally-assessed taxpayers could have come up with values lower than Mr. Dickerson' s proposed valuation of their property.

absent evidence of the fair market value of CSXT in 2001 or the fair market value of other taxpayers in 2002, the court cannot determine that CSXT has been singled out for discriminatory treatment.

Mr. Dickerson, moreover, testified that the largest part of the increase in CSXT's 2002 assessment was due to a change he instituted that year for all railroads, which was not needed for non-railroad public utilities. Specifically, he began using income data taken from CSX Corporation's annual reports instead of CSXT's R-1[27] reports to project future cash flows in his DCF analysis. Because those income figures can differ significantly from each other, the choice of which to use can greatly affect the DCF indicator of value. The evidence at trial showed that CSX Corporation's annual reports reflect management's view of CSXT's financial performance.

Finally, CSXT argues that the Department's treatment of other centrally-assessed taxpayers for the tax year 2004 is potent evidence that CSXT was singled out in 2002. In the tax year 2004, Mr. Dickerson devised a new way of calculating the risk premium for centrally-assessed taxpayers, which he then applied to his valuation worksheets for the tax year 2004. This new calculation increased the Department's initial valuation of the majority of centrally-assessed taxpayers, which, in turn, caused a "stir." The Department, in an attempt to avoid litigation, had a meeting with six representatives from centrally-assessed taxpayers, including CSXT. At the conclusion of the meeting, CSXT and the other five companies agreed that for the tax year 2004, all centrally-assessed taxpayers would receive an assessment equal to their assessment for the previous year or the average of their past three years of assessments, whichever was greater. For 2004, CSXT was assessed at $6.5 billion, a

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[27] An R-1 report is a report made by a railroad, such as CSXT, to the STB.

slight increase over the Department's 2001 assessment. Because the Department reverted to CSXT's 2001 values in 2004, CSXT argues that this is an indication that CSXT was singled out for different tax treatment in 2002 and 2003.

The Department's 2004 assessment of CSXT indicates little about the Department's 2002 valuation of CSXT. The Department negotiated an agreement with all public utilities in 2004 to avoid litigation. The agreement mandated that these taxpayers receive an assessment equal to their assessment for the previous year or the average of their past three years of assessments. As a practical matter, the Department could not have used either formula for CSXT because CSXT had filed suits challenging the Department's 2002 and 2003 valuations. The only avenue left to the Department was to revert to CSXT's 2001 assessment.

B. *Whether CSXT Has Been Treated Differently Than Norfolk Southern*

CSXT next argues that it has been treated differently than the only other major railroad in Georgia, Norfolk Southern. Like CSXT, Norfolk Southern filed suit against the defendants challenging the Department's 2002 assessment. The Department, however, settled Norfolk Southern's lawsuit and agreed to only minimal increases in value over the Department's 2001 assessment of Norfolk Southern. Ultimately, this meant that Norfolk Southern's 2002 value in Georgia was less than $8.2 billion.

CSXT argues that valuing Norfolk Southern less than CSXT for the tax year 2002 is wrong and discriminatory. CSXT points out that the Department consistently valued Norfolk Southern higher than CSXT for the tax years 2002-2004 and consistently projected higher cash flows for Norfolk Southern. If the Department truly believed that Norfolk Southern was worth more than CSXT, how, asks CSXT, could the Department assert in this suit that CSXT' s [sic]

value is higher than the agreed-to value of Norfolk Southern for the tax year 2002?

The court finds CSXT' s [sic] arguments unpersuasive. Nothing in the 4-R Act requires the court to compare the treatment of CSXT to just one company, another railroad. In *Atchison, Topeka, and Santa Fe Railway,* 78 F.3d at 442, the railroad argued that the court could measure whether Arizona's tax statutes discriminated against it solely by looking at the treatment of other motor carriers, as opposed to comparing all commercial and industrial taxpayers. The Ninth Circuit rejected this argument stating, "Although subsection(b)(4) is silent as to the proper comparison class, congressional intent behind the 4-R Act dictates that the comparison class of 'other commercial and industrial taxpayers subject to the tax' be used." *Id.*

The court finds the logic of the Ninth Circuit persuasive. By narrowing the comparison class to just one company, CSXT attempts to greatly expand the reach of the 4-R Act and increase the likelihood of future litigation. Accordingly, the court finds that it is improper to compare CSXT's treatment to just one other company, Norfolk Southern, for purposes of determining whether CSXT has been discriminated against in violation of the 4-R Act.

Even if it was proper to compare solely CSXT and Norfolk Southern, the court still finds that CSXT has not been singled out for discriminatory treatment. CSXT did not present any evidence that it was treated differently than Norfolk Southern when the Department made its initial proposed valuation of Norfolk Southern. If anything, the fact that Norfolk Southern also filed suit challenging the Department's proposed valuation suggests that Norfolk Southern was treated similarly to CSXT.

In addition, the fact that the Department ultimately settled with Norfolk Southern does not compel the court to conclude

that CSXT was treated differently from Norfolk Southern. Lawsuits are settled for numerous reasons, including the need to allocate scarce legal resources differently.

V. *Whether the Department Improperly Included the Value of CSXT's Intangible Property in Its Proposed Valuation in Violation of 49 U.S.C. § 11501(b)(4)*

CSXT's last claim is that the Department's Proposed Valuation includes amounts attributable to intangible property that is not taxed to locally-assessed taxpayers, resulting in a violation of 49 U.S.C. § 11501(b)(4). When a railroad is valued as a unit on a going concern basis, it is undisputed that the unit value of that railroad necessarily includes all of the railroad's assets, both tangible and intangible. The trend in a majority of states, however, is to exclude intangible property from ad valorem taxation. In 1996, the state of Georgia followed this trend and repealed its ad valorem tax on intangible property. *See* O.C.G.A. § 48-6-21. Thus, the intangible property of CSXT is not taxable in Georgia.

As an initial matter, the court must address the definition of the term "intangible property." Intangible property is generally defined as property that lacks a physical existence, such as stock options and business goodwill. *Black's Law Dictionary* 1253 (8th ed.2004). The court is not aware of any decision by the Georgia Department of Revenue or by Georgia courts that articulates a list of property included within the definition of "intangible property" for purposes of tax valuation. Under the repealed Georgia statute subjecting intangible property to an ad valorem tax, the Georgia legislature defined intangible property as:

(1) Money;

(2) Collateral Security Loans;

(3) Stocks;

(4) Accounts receivables and notes not representing credits secured by real estate;

(5) Bonds and debentures of all corporations;

(6) Long term notes secured by real estate;

(7) Short term notes secured by real estate;

(8) Restricted foreign intangibles;

(9) Patents, copyrights, franchises, and all other classes of intangible personal property not otherwise enumerated; and

(10) Computer software defined by statute.

O.C.G.A. § 48-6-21.

Although it has been repealed, O.C.G.A. § 48-6-21 is an indication that the Georgia legislature believed that the assets listed above constitute intangible property. Further, by repealing the statute, the legislature implicitly indicated that these types of intangible property were no longer subject to taxation. The court, therefore, finds that, at the very least, the list of property included in O.C.G.A. § 48-6-21 is a good starting point for defining the term "intangible property."

Despite the repeal of O.C.G.A. § 48-6-21, CSXT claims that its intangible property has been included within the Department's Proposed Valuation. The Department admits that its unit valuation of CSXT initially included CSXT' s [sic] tangible and intangible property, but claims that it deducted $400 million from its unit value to account for CSXT's intangible property.

Instead of attempting to identify and value its intangible property, CSXT contends that it is impractical to identify and value its intangible property, and, thus, the court should require the Department to use the yield capitalization approach, which CSXT contends does not compound intangibles. CSXT claims that the court should require the

defendants to use the yield capitalization approach because the Department's market multiple and stock and debt approaches allegedly unnecessarily compound intangible values.[28] For example, CSXT has presented evidence that a company's stock prices may increase when that company hires a new CEO. This increase in the stock price is not attributable to tangible assets. Because the stock and debt and the market multiple approaches both rely on a company's stock price,[29] they compound intangible assets.

As support for its argument that the court should adopt the yield capitalization approach, CSXT cites to a decision by the Utah Tax Commission ("Commission") in *WilTel, Inc. v. Beaver County*, Nos. 95-0789 and 95-0824 (Utah Tax Commission December 5, 1997)("*WilTel II*"). WilTel, Inc. is a provider of long-distance telecommunications services. In 1995, the Utah State Property Tax Division (the "Division") calculated WilTel's unit value based on the stock and debt and income approaches. WilTel appealed the assessment to the Utah Tax Commission and moved for partial summary judgment arguing, in part, that Utah's assessment improperly included intangible property, which was not taxable under Utah law. *WilTel, Inc. v. Beaver County*, No. 95-0789, 1997 Utah Tax LEXIS 111, at *2-3 (Utah Tax Commission April 21, 1997) ("*WilTel I*"). The Utah Tax Commission found that the income and stock and debt approaches tend to compound intangible values. The Utah Tax Commission then remanded the case to the parties to identify, value, and re-

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[28] It is undisputed here that the Department does not and did not intend to value the intangible property of other commercial and industrial property. It is also undisputed that all three of the valuation methods used by the Department initially included the value of CSXT's intangible property.

[29] For clarification purposes, unlike the stock and debt approach, the market multiple approach relies on the stock prices of comparable companies, as opposed to CSX Corporation's stock prices.

move WilTel's intangible property using the cost approach." *Id.* at *14-15.

On remand, the parties were unable to agree on the valuation of WilTel's tax-exempt intangible property, and, thus, the matter came before the Utah Tax Commission again for a formal hearing to determine the value of WilTel's intangible property. *WilTel II* at *2. The Commission finally concluded that "separately valuing intangibles and deducting them from a unit valuation is impractical." *WilTel II* at *3. In an attempt to minimize the inclusion of intangibles in the unit rule method, the Utah Tax Commission concluded that the parties should use a yield capitalization approach and a cost approach and that each approach should be weighted at 50%. The Utah Tax Commission then remanded the case to the Division to calculate the value of WilTel under a yield capitalization approach (minus growth) and to time adjust its cost approach. *WilTel II* at *6.

While the *WilTel II* decision is attractive because of its simplicity, the court finds that the reasoning of *WilTel II* is not appropriate in this case. First, this is a case brought under the 4-R Act, and not merely an appeal of a state tax valuation. The court has already held that CSXT may not challenge the Department's valuation methods in this case. If this court were to adopt the reasoning of *WilTel II*, the court would be dictating to the Department a particular valuation method.

Second, CSXT has not convinced the court that it is impossible or impractical to value its intangible property. While CSXT's local assessment expert, Ms. Judith Ross, testified that identifying and valuing a company's intangible property would be extremely difficult, she also testified that performing a unit valuation in general is difficult. Ms. Ross further testified that intangible property can be identified and valued by a person with expertise. Thus, the court finds that it is not impractical or impossible to identify and value CSXT's intangible property.

Third, while the court believes that the stock and debt approach undoubtedly includes value attributable to intangible property in its initial unit value, the court also finds that the yield capitalization method touted by CSXT includes some value attributable to intangible property. In fact, CSXT has admitted that Mr. Tegarden's yield capitalization value includes some value attributable to intangible property. This is further illustrated by the fact that CSXT deducts $400 million from Mr. Tegarden's unit value of CSXT—the same $400 million deduction that the Department took to account for certain intangibles owned by CSXT.

Fourth, this case differs[30] from the *Wiltel* decisions in that in *Wiltel I*, the Utah Tax Commission remanded the case so that the taxpayer could identify its intangible property. The parties, however, could not agree on the value of Wiltel's intangible property. In this case, CSXT has not even presented any evidence that it owns intangible property.

Here, it is undisputed that Mr. Dickerson deducted $400 million from his unit value of CSXT to account for certain intangibles. He testified that the $400 million deduction was his attempt to eliminate the value of CSXT's intangible property that was previously separately taxed under O.C.G.A. § 48-6-21. When asked why he did not attempt to value and deduct other intangible property from his initial assessment, Mr. Dickerson testified that CSXT did not present the Department with any evidence that CSXT owned other intangible property. Consistent with its statement to Mr. Dickerson, at trial CSXT failed to identify any specific intangible property

[30] The court also notes that holdings in the *WilTel* cases are not binding upon this court for numerous reasons: (1) the *Wiltel* decisions were made by the Utah State Tax Commission; (2) the taxpayer in the *Wiltel* cases was a telecommunications company, not a railroad; and (3) the *Wiltel* cases were not decided under the 4-R Act.

that it owned as of January 1, 2002.[31] CSXT also failed to present evidence as to how much its intangible property was worth. *Cf. Burlington N. R.R. Co. v. Huddleston*, 94 F.3d 1413, 1415 (10th Cir.1996) (in its complaint alleging a violation of the 4-R Act, the railroad also alleged that the value of its intangible property, computer software, was at least $8 million); *Bair*, 815 F.Supp. at 1239 (separately identifying and valuing intangible property of a railroad for purposes of 4-R Act claim). Nor has CSXT provided the court with any evidence that the Department's $400 million intangible property deduction was under-inclusive.

The court, therefore, concludes that CSXT has not carried its burden of showing by a preponderance of evidence that the Department improperly included intangible property in the Department's Proposed Valuation of CSXT.

Conclusion

For the reasons discussed above, the court concludes that the defendants have not discriminated against CSXT in violation of 49 U.S.C. § 11501(b)(4).

The court also holds that the true market unit value of CSXT for the tax year 2002 was $7,726,293,350.[32] The true market value of CSXT's taxable rail transportation property in Georgia for the tax year 2002 was $509,560,171.[33] The defendants, therefore, have not discriminated against CSXT

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[31] For example, CSXT did not provide the court with any evidence that it owns any trademarks, copyrights, or patents.

[32] The court arrived at this number by taking the Department's $8,126,293,350 DCF value for CSXT and subtracting $400 million to account for CSXT's intangible property.

[33] The court reached this number by taking the $7,726,293,350 true market unit value of CSXT and allocating 7.194059% to Georgia. The court then deducted $4,156,193 to account for CSXT's motor vehicles, $2,907,467 to account for pollution control, and $39,210,271 to account for W & A exempt line.

in violation of 49 U.S.C. § 11501(b)(1) because the ratio of assessed value to true market value of CSXT's property does not exceed the jurisdictional threshold set out in the 4-R Act of 42%. Thus, CSXT is not entitled to relief under the 4-R Act for the tax year 2002.

The clerk is DIRECTED to close this file and issue judgment for the defendants in accordance with this order.

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

CIVIL ACTION FILE NO. 1:02-cv-2634-CAP

CSX TRANSPORTATION, INC.,
Plaintiff,

vs.

THE STATE BOARD OF EQUALIZATION
OF THE STATE OF GEORGIA; *et. al.*
Defendant.

JUDGMENT

This action having come before the court, Honorable Charles A. Pannell, Jr., United States District Judge, for consideration it is

Ordered and Adjudged that the Defendants have not discriminated against CSXT in violation of 49 U.S.C. § 11501(b)(1). This action is dismissed.

Dated at Atlanta, Georgia, this 29th day of September, 2005.

LUTHER D. THOMAS
CLERK OF COURT

By: /s/ Don Stanhope
Deputy Clerk

UNITED STATES COURT OF APPEALS
ELEVENTH CIRCUIT

No. 05-16000

CSX TRANSPORTATION, INC.,
Plaintiff-Appellant,

v.

STATE BOARD OF EQUALIZATION, of the State of Georgia, JERRY JACKSON, as Commissioner of Revenue of the State of Georgia, RUSSELL W. HINTON, as State Auditor of the State of Georgia, RAY J. CRAWFORD, as Director of the Georgia State Properties Commission
Defendants-Appellees.

Dec. 19, 2006

Appeal from the United States District Court
for the Northern District of Georgia.

Before BIRCH, PRYOR and FAY, *Circuit Judges.*

PRYOR, *Circuit Judge:*

This appeal presents a question about state taxation of railroad properties that was expressly left open by the Supreme Court of the United States, has since divided the federal appellate courts, and involves the traditional balance of federal and state power. We are asked to decide whether section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 (4-R Act or the Act), 49 U.S.C. § 11501, allows a railroad to challenge the methodology by which a state determines the true market value of railroad property for *ad valorem* tax purposes. The 4-R Act provides an exception to the general rule of the Tax Injunction Act that federal

district courts will not interfere with matters of state taxation. *Compare id. with* 28 U.S.C. § 1341. This appeal turns on the breadth of that exception.

CSX Transportation, Inc. (the Railroad) filed a complaint against the State Board of Equalization of Georgia (the Board), under section 306 of the Act, in which it challenged the appraisal of its property by the Board at $8.2 billion. Section 306 requires, for purposes of levying a property tax, that the ratio of assessed value to true market value of railroad property not exceed by more than five percent the ratio of assessed value to true market value of all other commercial and industrial property in the same assessment jurisdiction. 49 U.S.C. § 11501(c). The district court refused to consider an appraisal proffered by the Railroad that valued the property of the Railroad at $6 billion because the district court concluded that the appraisal was based on a valuation methodology different from the one used by the State. *CSX Transp. v. State Bd. of Equalization*, 448 F.Supp.2d 1330, 1348 (N.D.Ga.2005). The Railroad argues that the 4-R Act allows it to challenge the valuation methodology of a state. Because the Act does not clearly state that railroads may challenge state valuation methodologies, we affirm the judgment of the district court.

I. BACKGROUND

The Railroad is a wholly-owned subsidiary of CSX Corporation. In tax year 2002, the Railroad provided freight transportation over a network that included a route through the State of Georgia. In Georgia, public utilities are centrally-assessed taxpayers, and public utilities include railroads, investor-owned electric utilities, investor-owned telephone companies, pipeline companies, and gas distribution companies. Although most taxpayers in Georgia are assessed, in the first instance, by county boards of assessors, the State Revenue Commissioner issues proposed assessments of the property of centrally-assessed taxpayers for each county in

which the taxpayer owns taxable property. The Property Tax Division of the Georgia Department of Revenue (the Department) prepares a digest of public utility assessments that the Board reviews and approves. The Board then certifies the proposed assessments to each county in which taxable property is owned. Ga.Code Ann. § 48-2-18(c). Each county "may, but is not required to, use these figures as the county's own tax assessment." *Colonial Pipeline Co. v. Collins*, 921 F.2d 1237, 1240-41 (11th Cir.1991). For 2002, 59 of the 71 Georgia counties in which the Railroad owned taxable property adopted the proposed assessment of the Board.

In 2002, as in preceding years, the Department determined the value of all public utilities using the unit rule. Under this rule, an appraiser first determines the value of all assets of an entity, regardless of location. That amount is then multiplied by the percentage of the entity located within Georgia to determine what portion of the value of the company should be allocated to the state. The Railroad agrees that the unit rule is a proper method of valuation under Georgia law.

Although there are several different methods for determining the value of a company or property under the unit rule, those methods fall into three general categories: the sales comparison approach, the cost approach, and the income approach. Under a sales comparison approach, a company or property is appraised by examining actual sales of comparable companies or properties. Under the cost approach, an appraiser adds together the original costs of the various components of a company or property and makes deductions for depreciation or obsolescence. Under an income approach, an appraiser determines the future income stream of a company or property over the life of the company or property.

Gregg Dickerson prepared the valuation worksheets for the appraisal of the Railroad in 2002. Dickerson was an appraiser with 30 years of experience, including experience regarding the use of the unit rule in public utility valuation.

Dickerson performed unit valuations at the Department for ten years before leaving in 1993 to work in the tax department at Norfolk Southern Railroad. Dickerson returned to the Department in 2001 to serve as the Program Manager of its Public Utilities section.

When Dickerson returned to the Department, he altered the combination of valuation methods the Department used to calculate value under the unit rule. The Department had been calculating the unit values of all public utilities using a yield capitalization method (an income approach), a direct capitalization method (another income approach), and a stock and debt method (a sales comparison approach). For tax year 2002, Dickerson replaced the first two methods with a discounted cash flow method (an income approach) and a market multiples method (a sales comparison approach). Dickerson retained the third method.

Dickerson appraised the property of the Railroad using these three methods. He first used the stock and debt method, which assumes that the value of a company equals the sum of its outstanding debt and its equity. Under this method, Dickerson's appraisal was $12.022 billion.

Dickerson next used the discounted cash flow method. Under this method, an appraiser first projects the cash flows of a company for a designated number of years after the assessment date and discounts those expected cash flows to their present value. The appraiser then calculates a terminal or reversion value that represents the value of the company at the end of the projection period. These two values together give the appraiser his unit value for the company. Dickerson calculated four terminal values using different indicators of reversion. The unit value calculated using a terminal growth rate of 63 percent was the lowest of the four, and Dickerson selected that value. Dickerson's appraisal, under this method, was $8,126,293,350.

Finally, Dickerson used the market multiples method. This method requires an appraiser to derive market multiples from the stock prices of companies engaged in similar lines of business and compare those multiples with the subject company to determine its value. Dickerson performed three different market multiples analyses, which resulted in appraisals of $12.346 billion, $10.769 billion, and $8.474 billion.

The five values derived from these three methods gave Dickerson a valuation range of $8.126 to $12.346 billion. As he did with all public utilities that year, Dickerson selected an amount at the lower end of that range to avoid potential litigation. Dickerson selected $8.2 billion as the lower limit of what the unit value of the Railroad might reasonably be. He then deducted $400 million to account for intangible property not subject to *ad valorem* taxation. Ga.Code Ann. § 48-6-21. The adjusted unit value of $7.8 billion was multiplied by 7.194059 percent, which was the percentage of the track of the Railroad located in Georgia, which resulted in an allocated value of $561,136,602. Dickerson made further deductions for motor vehicles, pollution control equipment, and an exempt rail line, and he arrived at a taxable fair market value of $514,862,672.

The Railroad filed a complaint under the 4-R Act that challenged the valuation proposed by the Department. The Act bars states from discriminating against railroads when levying property taxes:

> The following acts unreasonably burden and discriminate against interstate commerce, and a State, subdivision of a State, or authority acting for a State or subdivision of a State may not do any of them:
>
> (1) Assess rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in

> the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
>
> (2) Levy or collect a tax on an assessment that may not be made under paragraph (1) of this subsection.
>
> (3) Levy or collect an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.
>
> (4) Impose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the Board under this part.

49 U.S.C. § 11501(b).

When a violation of the 4-R Act reaches a certain quantitative threshold, redress is allowed as an exception to the Tax Injunction Act, 28 U.S.C. § 341, which ordinarily bars challenges of state taxation practices in federal courts:

> Notwithstanding section 1341 of title 28 and without regard to the amount in controversy or citizenship of the parties, a district court of the United States has jurisdiction, concurrent with other jurisdiction of courts of the United States and the States, to prevent a violation of subsection (b) of this section. Relief may be granted under this subsection only if the ratio of assessed value to true market value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction. The burden of proof in determining assessed value and true market value is governed by State law.

49 U.S.C. § 11501(c).

The Railroad argued that it was taxed at a higher ratio of assessed value to true market value than other commercial

and industrial property, in violation of section 11501(b)(1), because the true market value of its property for 2002 did not exceed $6 billion. The Railroad submitted an appraisal prepared by Thomas Tegarden, whose credentials the district court described as "impeccable." *CSX Transp.*, 448 F.Supp.2d at 1333. Tegarden used three valuation methods, two of which had not been used by the Department: a stock and debt method, a cost method, and a yield capitalization method. These methods produced valuations of $9.367 billion, $6.15 billion, and $5.983 billion, respectively. Tegarden gave no weight to his stock and debt value, little weight to his cost value, and primary weight to his yield capitalization value, and concluded that the unit value of the Railroad for tax year 2002 did not exceed $6 billion. Tegarden made the same adjustments as the Department for intangible property, motor vehicles, pollution control equipment, and the exempt rail line, and applied the same track-mile percentage, which resulted in a taxable fair market value of not more than $369,253,752.

The district court concluded that it was not permitted to consider Tegarden's appraisal. The district court interpreted the 4-R Act to bar consideration of appraisals based on a valuation methodology different from the methodology used by the State, unless the methodology of the State is irrational or intentionally discriminatory. *Id.* at 1342. The court rejected the argument that Tegarden's valuation methodology was a variant of the same methodology used by the State. *Id.* at 1343.

The Railroad also challenged the accuracy of several calculations by the Department in its appraisal. In one of these challenges, the Railroad argued that the Department erred in using 6.3 percent as the terminal growth rate in its discounted cash flow valuation. The terminal growth rate plays a central role in determining the terminal or reversion value in the discounted cash flow method of valuation.

Dickerson testified that he chose this rate because it is the long-term growth rate of the gross domestic product and is the type of rate the market would use to estimate the terminal value of a company using a discounted cash flow method. The Railroad argued that this rate was higher than the growth rate used to project cash flows through 2011 (the first half of the discounted cash flow valuation) and, because the Department projected that the revenue of the Railroad would grow at only 2 percent, a growth rate of 6.3 percent would require that expenses become negative.

The district court found that the testimony of the experts of the Railroad on this issue lacked credibility. *Id.* at 1345. The court also found that these experts never stated what the growth rate should actually be. At most, their testimony suggested the Department should have used a rate of 3.5 percent or 4.5 percent, but the court concluded that these rates suffered from the same infirmities as the 6.3 percent rate, including that they would require expenses to become negative. *Id.*

After rejecting the arguments of the Railroad, the district court concluded that the true market value of the Railroad for tax year 2002 was $7,726,293,350. *Id.* at 1350. The court found the figure produced by the discounted cash flow method to be the most accurate appraisal of the value of the Railroad, and the court subtracted $400 million from the discounted cash flow value of the Department ($8,126,293,350) to account for intangible property. *Id.* at 1350 n. 23. The court concluded that the ratio of assessed value to true market value of the property of the Railroad did not exceed by more than five percent the ratio of assessed value to true market value of the other commercial and industrial property in the assessment jurisdiction of the Railroad. *Id.* at 1350. The district court entered a judgment in favor of the Board.

II. STANDARDS OF REVIEW

We review factual findings of the district court for clear error and conclusions of law *de novo*. *Glassroth v. Moore*, 335 F.3d 1282, 1296-97 (11th Cir.2003).

III. DISCUSSION

The Railroad raises three challenges to the determination by the district court of its true market value for tax year 2002. The Railroad first contends that the district court erred in holding that the 4-R Act bars a railroad from challenging the valuation methodology chosen by a state. Second, the Railroad argues that, even if it is barred from challenging the methodology of the Board, the appraisal of Tegarden should have been considered by the district court because that appraisal was based on the same methodology used by the Board. Third, the Railroad maintains that the district court clearly erred in accepting the use by the Board of a terminal growth rate of 6.3 percent in its discounted cash flow valuation. We address each argument in turn.

A. The 4-R Act Does Not Allow a Railroad to Challenge the Methodology by Which a State Determines Fair Market Value.

Whether a railroad may challenge, under the 4-R Act, the valuation methodology of a state is a question the Supreme Court has acknowledged but not decided. When it first interpreted the 4-R Act in *Burlington Northern Railroad v. Oklahoma Tax Commission*, the Court held that a railroad need not prove intentional discrimination to challenge factual determinations made by a state in the application of its valuation methodology. 481 U.S. 454, 462-63, 107 S.Ct. 1855, 1860-61, 95 L.Ed.2d 404 (1987). In a footnote, the Court expressly refrained from deciding whether the Act allows a railroad to challenge the valuation methodology itself:

> This case therefore does not present the question whether a railroad may, in an action under § 11503 [now

> § 11501], challenge in the district court the appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied. Accordingly we express no view on that issue.

Id. at 463 n. 5, 107 S.Ct. at 1861 n. 5.

Three of our sister circuits, following *Burlington Northern v. Oklahoma*, have split on whether railroads may challenge state valuation methodologies. The Fourth Circuit, on the one hand, has concluded that the 4-R Act does not permit a railroad to challenge the valuation methodology of a state. That circuit concluded that the text of the Act is ambiguous, and the court was "not inclined to disregard" the general policy of noninterference in matters of state taxation contained in the Tax Injunction Act "where § 306 does not plainly authorize such an exception." *Chesapeake W. Ry. v. Forst*, 938 F.2d 528, 531 (4th Cir.1991); *accord Richmond, Fredericksburg & Potomac R.R. Co. v. Forst*, 4 F.3d 244, 250 (4th Cir.1993). The Second and Ninth Circuits, on the other hand, have repudiated *Chesapeake Western* and held that railroads may challenge valuation methodologies. In *Burlington Northern Railroad v. Department of Revenue*, the Ninth Circuit explained that section 11501(c) of the 4-R Act provides that state law governs the burden of proof in challenges to assessed value and true market value. 23 F.3d 239, 241 (9th Cir.1994). Because determinations of property value by public officials in the State of Washington may be defeated by "clear, cogent and convincing evidence," the court reasoned that state valuation methodologies may likewise be defeated by clear, cogent, and convincing evidence. *Id.* In *Consolidated Rail Corp. v. Town of Hyde Park*, the Second Circuit held that, at least where states use a unique method to appraise railroads, the 4-R Act allows railroads to challenge valuation methodology. 47 F.3d 473, 482 (2d Cir.1995).

The Railroad argues that *Chesapeake Western* was wrongly decided and urges us to follow *Burlington Northern v. Department of Revenue* and *Consolidated Rail* in allowing railroads to challenge valuation methodology. The Railroad contends that the 4-R Act allows a challenge of any act, including the choice of a methodology, that has the effect of discriminating against railroads. The Railroad relies on the statement of the Court in *Burlington Northern v. Oklahoma* that the Act "speaks only in terms of 'acts' which 'unreasonably burden and discriminate against interstate commerce'; nowhere does it refer to the intent of the actor." 481 U.S. at 463, 107 S.Ct. at 1861.

The Railroad also relies on broad statements in previous decisions of our Court. The Railroad reminds us that we have stated that "[t]he legislative history and broad language of the Act show Congress possessed a general concern with discrimination in all of its guises." *S. Ry. v. State Bd. of Equalization*, 715 F.2d 522, 528 (11th Cir.1983). We also have stated that "Congress meant unconditionally to ensure a federal forum for section 11503 [now section 11501] claims." *Id.* at 527.

Notwithstanding our earlier dicta to the contrary, we are persuaded that the Fourth Circuit correctly interpreted the 4-R Act as being subject to a clear statement rule. It is a well-settled principle of statutory interpretation that a statute will not be construed to burden states in the exercise of their traditional powers unless it clearly states its intent to do so. "'If Congress intends to alter the usual constitutional balance between the States and the Federal Government, it must make its intention to do so unmistakably clear in the language of the statute.'" *Gregory v. Ashcroft*, 501 U.S. 452, 460-61, 111 S.Ct. 2395, 2401, 115 L.Ed.2d 410 (1991) (quoting *Atascadero State Hosp. v. Scanlon*, 473 U.S. 234, 242, 105 S.Ct. 3142, 3147, 87 L.Ed.2d 171 (1985)). "This plain statement rule is nothing more than an acknowledgment that the States

retain substantial sovereign powers under our constitutional scheme, powers with which Congress does not readily interfere." *Id.* at 461, 111 S.Ct. at 2401.

Perhaps the most fundamental power of a sovereign is the power to tax. This power was originally considered so integral a power of the states as to admit of no abridgement by the federal government, *see* The Federalist No. 32 (Alexander Hamilton), and its singular importance to the states has been repeatedly acknowledged. *See Dep't of Revenue v. ACF Indus.*, 510 U.S. 332, 345, 114 S.Ct. 843, 850, 127 L.Ed.2d 165 (1994) (power to tax is "central to state sovereignty"); *Bode v. Barrett*, 344 U.S. 583, 585, 73 S.Ct. 468, 470, 97 L.Ed. 567 (1953) (power of a state to tax is "basic to its sovereignty"); *Curry v. McCanless*, 307 U.S. 357, 366, 59 S.Ct. 900, 905, 83 L.Ed. 1339 (1939) (power to tax is "incident to" and "coextensive with" sovereignty). This understanding of the relationship of sovereignty and taxation is implicit: "It is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments." *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110, 20 L.Ed. 65 (1871).

The selection of a valuation methodology is part of this fundamental power of a state. *See Louisville & Nashville R.R. v. Dep't of Revenue, Fla.*, 736 F.2d 1495, 1498 (11th Cir.1984) ("These arguments broach delicate issues implicating the state's traditional authority to select methods of valuation."). Important questions of state policy are often intertwined with the selection of a valuation methodology. Time pressures and limited resources, for example, may compel a state to choose a simple valuation methodology rather than a complicated one. *See, e.g., Union Pac. R.R. v. State Tax Comm'n*, 716 F.Supp. 543, 557 (D.Utah 1988).

The Supreme Court has "long recognized that principles of federalism and comity generally counsel that courts should adopt a hands-off approach with respect to state tax admin-

istration." *Nat'l Private Truck Council v. Okla. Tax Comm'n*, 515 U.S. 582, 586, 115 S.Ct. 2351, 2354, 132 L.Ed.2d 509 (1995). Because the states rely so heavily on their ability to tax, "'it is of the utmost importance to all of them that the modes adopted to enforce the taxes levied should be interfered with as little as possible.'" *Id.* (quoting *Dows*, 78 U.S. (11 Wall.) at 110). When Congress enacted the Tax Injunction Act, it "intended to codify this pre-existing federal equity practice and to ensure more uniform adherence to the underlying principles of comity." *S. Ry.*, 715 F.2d at 527; *see also 28 E. Jackson Enters. v. Cullerton*, 523 F.2d 439, 441 (7th Cir.1975) (Tax Injunction Act "codifies the well-established federal policy of noninterference in matters of state taxation").

The Railroad argues that principles of federalism and comity should play no role in our interpretation of the 4-R Act. This argument is not new. We have stated that "Congress intended to carve out an exception not only to the Tax Injunction Act, but also to the underlying doctrine of equitable restraint in the narrow area of discriminatory taxation of railroads," *S. Ry.*, 715 F.2d at 529, and the Eighth Circuit has stated that "[t]he common law principle of federal deference to state tax schemes, as amplified by 28 U.S.C. § 1341, has no place in a § 306 analysis," *Burlington N. R.R. v. James*, 911 F.2d 1297, 1300 (8th Cir.1990).

The problem with this argument is that more recently the Supreme Court has stated the opposite. In a decision mentioned by neither the Ninth Circuit in *Burlington Northern v. Department of Revenue* nor the Second Circuit in *Consolidated Rail*, the Supreme Court ruled in 1994 that states may grant exemptions from a generally applicable *ad valorem* property tax without subjecting the taxation of railroad property to challenge under subsection (b)(4) of the Act. *ACF Indus.*, 510 U.S. at 335, 114 S.Ct. at 846. The Court reached this conclusion based on the text of the Act, *id.* at

339-43, 114 S.Ct. at 848-50, and then explained, "Principles of federalism support, in fact compel, our view. Subsection (b)(4), *like the whole of § 11503* [now § 11501], sets limits upon the taxation authority of state government, an authority we have recognized as central to state sovereignty," *id.* at 345, 114 S.Ct. at 850 (emphasis added). The Court stated that principles of federalism required the use of a clear statement rule in this context. *Id.* at 345, 114 S.Ct. at 850-51. Because it was not the "clear and manifest purpose of Congress" to allow railroads to challenge property tax exemptions in federal court, the Court refused to read the 4-R Act as granting them that right. *Id.*

Based on the reasoning of the Court in *ACF Industries*, we conclude that railroads may not challenge state valuation methodologies under subsection (b)(1). The text of the Act does not clearly state that railroads may challenge valuation methodologies. Without that clear statement of congressional intent, the argument of the Railroad fails.

The legislative history, "to the extent it has any relevance to our inquiry," *ACF Indus.*, 510 U.S. at 345, 114 S.Ct. at 851, supports the conclusion that railroads may not challenge state valuation methodologies in federal court. The committee report regarding a precursor of section 306 explained that the bill "does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves. It merely provides a single standard against which all affected assessments must be measured." S.Rep. No. 90-1483, app. B, at 22 (1968). The testimony of a railroad representative at a hearing on an earlier version of section 306 was consistent with this interpretation: "The standards and methods of valuation that any State wishes to use would be unaffected by this legislation." *Hearing on H.R. 16245 Before the Subcomm. on Transp. & Aeronautics of the H. Comm. on Interstate & Foreign Commerce*, 91st Cong. 138 (1970) (statement of Philip M. Lanier).

The most that can be said for the argument of the Railroad is that it was articulated ably in the dissenting opinion in *ACF Industries*. Justice Stevens argued that "the text of subsection (b)(4) and its evident purposes convince me that Congress intended to bar discrimination by any means, including exemptions." *ACF Indus.*, 510 U.S. at 350, 114 S.Ct. at 853 (Stevens, J., dissenting). The lower court that the Supreme Court in *ACF Industries* reversed also reached this conclusion. *See id.* at 338, 114 S.Ct. at 847 ("The court [of appeals] explained that Congress enacted § 11503 [now § 11501] to 'prevent tax discrimination against railroads *in any form whatsoever.*'" (citation omitted)). We obviously are not at liberty to follow either Justice Stevens's dissenting opinion or the decision reversed by the Supreme Court. The district court was not allowed to consider a valuation methodology different from the methodology of the Board.

B. The District Court Did Not Clearly Err in Finding That the Railroad Used a Valuation Methodology Different From the Methodology of the State.

The Railroad and an amicus curiae argue, in the alternative, that the appraisal by Tegarden was based on the same methodology used by the State. The American Association of Railroads, as amicus curiae, argues that there is a tri-partite taxonomy of appraisal terminology consisting in unit rule and summation "methodologies"; income, cost, and market "approaches" for determining value under the unit rule; and stock and debt, discounted cash flow, yield capitalization, and other "techniques" for implementing the various approaches. Under this taxonomy, our decision in subsection III.A would bar the Railroad from challenging only the adoption of the unit rule.

Although this taxonomy may be useful within the appraisal community, there is little legal support for this argument. The Association argues that the Fourth Circuit has used the terms "method" and "methodology" in the way it advocates,

see Chesapeake W. Ry., 938 F.2d at 529, but other courts have used those terms to designate more specific components of the valuation process. *See, e.g., Consol. Rail*, 47 F.3d at 477 (discussing "the 'income capitalization method'" and "the 'stock and debt method'"); *Union Pac. R.R.*, 716 F.Supp. at 551 (referring to "yield capitalization" and "direct capitalization" as different methods and methodologies).

The more serious problem for the Association is that its argument is contrary to the understanding of the Supreme Court. A close reading of footnote 5 of *Burlington Northern v. Oklahoma* establishes that the Supreme Court understands the phrase "accounting methods" to encompass all nonfactual determinations made in the process of appraising a railroad. We quote the text of that footnote as follows, with our emphasis on three key phrases:

> This case therefore does not present the question whether a railroad may, in an action under § 11503 [now § 11501], challenge in the district court the appropriateness of the *accounting methods* by which the State determined the railroad's value, *or is instead restricted* to challenging the *factual determinations* to which the State's preferred accounting methods were applied. Accordingly we express no view on that issue.

481 U.S. at 463 n. 5, 107 S.Ct. at 1861 n. 5 (emphasis added).

This language suggests that there are only two categories in the valuation process, and the Court understood "accounting methods" and "factual determinations" to be exhaustive of all possibilities. It would not make sense to say that railroads, if barred from challenging accounting methods, would be "instead restricted" to challenging factual determinations if there were some third category in the valuation process, such as an "approach" or "technique," as the Association argues. The inability of railroads to challenge accounting methods restricts the railroads to challenging factual determinations.

The term "accounting methods" and the parallel term "valuation methodology" as used by the Supreme Court encompass all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be.

The definition of a "methodology" also should be understood in the light of the principles of federalism that govern our interpretation of the 4-R Act. Under the taxonomy advanced by the Association, a railroad would be barred from challenging the decision to use the unit rule, but permitted to challenge the use of a combination of the stock and debt method and a market multiples approach instead of a yield capitalization method and a cost approach. We are reluctant to allow that kind of freewheeling judicial second-guessing, which implicates delicate matters of state policy, *cf. Union Pac. R.R.*, 716 F.Supp. at 557 (explaining what might influence a choice between a direct capitalization and a yield capitalization method), without clear support in the text of the Act. We would expect Congress to state unambiguously its intention to subject states to challenges of both kinds of decisions in federal court.

Based on our understanding of the term "methodology," the district court did not clearly err in finding that the appraisal prepared for the Railroad by Tegarden was based on a methodology different from the methodology used by the State. The State appraised public utilities in 2002 by calculating five values under three different methods and selecting a figure at the low end of the resulting range. Tegarden calculated three values using three methods, only one of which had been used by the State. Instead of selecting a figure at the low end of his resulting range, Tegarden weighted each result, giving primary weight to one of the methods—yield capitalization—not used by the State. Even if the Railroad were able to convince us that the yield capitalization and discounted cash flow methods are alge-

braically the same, this conclusion would not establish that Tegarden used the same valuation methodology as the State. The State did not give primary weight—or any weight—to its discounted cash flow valuation. The selection by the Department of an appraisal amount nearest to the discounted cash flow number did not reflect the conclusion that discounted cash flow was the most accurate of the methods used, only that it was the lowest.

C. The District Court Did Not Clearly Err When It Accepted the 6.3 Percent Terminal Growth Rate Used by the State.

Finally, there was no clear error by the district court in its finding that the use of a terminal growth rate of 6.3 percent by the Board, in its discounted cash flow valuation, was acceptable. A factual finding "is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-74, 105 S.Ct. 1504, 1511, 84 L.Ed.2d 518 (1985) (internal quotations and citations omitted). We cannot say definitively that the district court made a mistake because its finding rested on issues of expert credibility.

Although the experts employed by the Railroad testified that a terminal growth rate of 6.3 percent was too high, Dickerson explained why he found it to be appropriate, including that 6.3 percent is the long-term growth rate of the gross domestic product. The district court stated that it found the experts of the Railroad to lack credibility on this issue. *CSX Transp.*, 448 F.Supp.2d at 1345. We have previously said that we "should be reluctant to overturn the district court's findings" where those findings are based on "crucial evaluations of witness credibility, particularly where the expert testimony conflicted." *L&C Marine Transp., Ltd. v. Ward*, 755 F.2d 1457, 1461 (11th Cir.1985).

The district court also based its finding on the failure of the Railroad to state what the terminal growth rate should be. *CSX Transp.*, 448 F.Supp.2d at 1345. At most, the testimony of its experts suggested that the Department should have adopted 3.5 percent or 4.5 percent as the terminal growth rate. *Id.* Even then, as the district court found, these rates suffered from the same alleged infirmities as the rate of 6.3 percent chosen by Dickerson, including that the rates would require expenses to become negative. *Id.* Based on this record, the district court did not clearly err.

IV. CONCLUSION

The judgment of the district court is

AFFIRMED.

FAY, *Circuit Judge*, concurring in part and dissenting in part:

As set forth in the majority opinion, the Railroad raises three issues in this appeal. The majority rejects all three of the Railroad's contentions. I agree that issues two and three have no merit. The district court did not err in finding Tegarden's appraisal was not based upon the same methodology as that used by the Board nor in accepting the 6.3 percent terminal growth rate used by the Board in its discounted cash flow evaluation.

Most respectfully, however, I disagree with the majority's holding that the 4-R Act bars the Railroad from challenging the valuation methodology chosen by the state. As acknowledged by the majority, our sister circuits have split on this issue. This gives me a little concern because in my opinion there is nothing ambiguous or complicated about these statutes.

Congress passed the Tax Injunction Act, 28 U.S.C. § 1341, which federal courts have enforced with great zeal. Congress, just as clearly, enacted the Railroad Revitalization and Regulatory Reform Act of 1976 (4-R Act), 49 U.S.C. § 11501, to correct a perceived evil; to wit: discriminatory tax practices by the states upon our national rail transportation system. The 4-R Act is a specific exception and excluded from the provisions of the Tax Injunction Act. 49 U.S.C. § 11501(c).

The language of the statute is straightforward and prohibits states from assessing rail transportation property at a value that has a higher ratio to the true market value than the ratio that the assessed value of other commercial and industrial property has to its true market value. If such a variation exists and exceeds five percent, relief may be granted to the railroad.

The only reference dealing with how such may be shown is a sentence that specifies that "the burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. § 11501(c). It is apparent from the record in this case that there are many methodologies that can be used in assessing the value of property. No one has suggested that Georgia law approves of some and disapproves of others.[1] Surely a state could not use one method to assess

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[1] A quick glance at some Georgia cases shows that the method of appraising value is often in dispute. See *Rogers v. De Kalb County Bd. of Tax Assessors*, 247 Ga. 726, 279 S.E.2d 223 (Ga.1981), where the plaintiff sought an injunction prohibiting the Board of Tax Assessors from using the published market (i.e., "blue book") value to assess his aircraft and requiring them to value and assess the aircraft on the basis of original cost minus depreciation, the method more commonly employed to value business equipment, furniture and fixtures. The plaintiff argued that aircraft represented tangible property just as business equipment, furniture and fixtures did, and that Georgia law required uniform taxation of property within the same class. The Georgia Supreme Court held that: "it is not '[im]permissible under the uniformity of taxation provision of the constitution to apply different methods of arriving at the fair market value of tangible property.'" *Id.* at 728, 279 S.E.2d 223, (citing *Wade v. Ray*, 234 Ga. 234 (214 S.E.2d 923) (1975)). See also *Chilivis v. Backus*, 236 Ga. 88, 90 (222 S.E.2d 371) (1976), where the Supreme Court of Georgia reviewed a lower court ruling that prohibited the county tax assessor from considering any factor other than actual use in arriving at fair market value. Holding that actual use is a determinative, but not exclusive, factor for determining a property's fair market value, the Court observed that: "[t]he object of the assessors must be to determine the fair market value of the property subject to taxation in the county and the methods employed may be varied if the object is attained." See also *Colvard v. Ridley*, 218 Ga. 490, 128 S.E.2d 732 (1962), where the taxpayer alleged that the tax assessors had taxed their real and personal property according to different methods, violating the state mandate for uniform taxation within a given class of property. The Supreme Court of Georgia held that: "[w]hile tax assessors were permitted a wide range of tools of placing a value on property, they were required to use the same valuation tool when placing a value on property within one class." *Id.* at 491, 128 S.E.2d 732. Finally, see *Inland Container Corp. v. Paulding County Bd. of Tax Assessors*, 220 Ga.App. 878, 470 S.E.2d 702 (Ga.Ct.App.1996), where two corporate

the market value of railroad property and a different method to assess other commercial and industrial property if such resulted in gross discrimination toward the railroad.

As articulated by the Second Circuit, such a situation would be in direct conflict with the clear meaning of the statute:

> 4. Method of Appraisal
>
> Relying primarily on a decision by the fourth circuit in *Chesapeake Western Ry. v. Forst*, 938 F.2d 528 (4th Cir.1991), the SBEA contends that Conrail is bound by the method of appraisal that the SBEA has chosen, and that since it chose to use the cost approach, it is improper to consider any other method of valuation in fixing the "true market value" of Conrail's properties. The *Chesapeake* court viewed the method of appraisal as a matter of state policy that was beyond the reach of the 4-R Act. We do not accept that interpretation of the statute. What the 4-R Act prohibits is discrimination against railroads in the ratios of two sets of numbers: assessed values and true market values of the railroad's property vis a vis those of other commercial and industrial properties. To avoid the prohibited discrimination, the SBEA must apply the same valuation standards and methods to the railroad property as are used on the commercial and industrial properties to which it is compared. If the Act were to be interpreted, as defendants would have it, so that the SBEA could adopt a special appraisal method for railroads alone, then

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landowners challenged their property tax assessments, arguing that the assessors should have considered "existing use" of the property. Noting that it could only judge the sufficiency of the evidence, not its weight, the Georgia Court of Appeals cautioned, "[n]or may we accept or reject any opposing methods of appraisal presented at trial." *Id.* at 881, 470 S.E.2d 702.

> the whole nondiscrimination objective of the statute could be circumvented.

Consolidated Rail Corp. v. Town of Hyde Park, 47 F.3d 473, 481-82 (2nd Cir.1995).

Since the objective of any methodology is a determination of *true market value,* a railroad should be allowed to challenge the method used in an attempt to prove that the result of such a method was not the *true market value* of its property. In sum, I agree with Justice Stevens that "the text of (the statute) . . . and its evident purposes convince me that Congress intended to bar discrimination by any means . . ." *ACF Industries*, 510 U.S. at 350, 114 S.Ct. at 853 (Stevens, J., dissenting). If the Railroad can prove that the method used by the state does not result in a fair appraisal of true market value and that the assessed value is in fact at a ratio higher than five percent of the ratio of true market value and assessed value of other commercial and industrial property, it is entitled to relief.

Having said all of this, I have no idea whether in this case the Railroad can meet its burden of proof. Although the district court found the Railroad's expert well qualified, other comments raise serious concerns about the weight that would have been given to the opinions expressed. I simply disagree with the absolute preclusion of any challenge to the methodology used by the state in arriving at the true market value of the Railroad's property.

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No. 06-1287

IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION of the State of Georgia; Bart L. Graham, as Commissioner of Revenue of the State of Georgia; Russell W. Hinton, as State Auditor of the State of Georgia; and Gena L. Abraham, as Director of the Georgia State Properties Commission,

Respondents.

On a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

BRIEF OF PETITIONER

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
MATTHEW J. WARREN
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Avenue, NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON, BEARMAN, CALDWELL & BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

* Counsel of Record

July 30, 2007

QUESTION PRESENTED

Whether, under the federal statute prohibiting state tax discrimination against railroads, 49 U.S.C. § 11501(b)(1), a federal district court determining the "true market value" of railroad property must accept the valuation method chosen by the State.

PARTIES TO THE PROCEEDINGS

All parties are listed in the caption.

RULE 29.6 STATEMENT

CSX Transportation, Inc. has a parent company, CSX Corporation, which is publicly traded. No other publicly held company owns more than 10% of petitioner's stock.

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OPINIONS BELOW

The order and judgment of the Court of Appeals, reported at 472 F.3d 1281 (11th Cir. 2006), appears at Joint Appendix ("JA") 244-266; see also Petition Appendix ("Pet. App.") 1a-23a. The order of the United States District Court for the Northern District of Georgia, which is reported at 448 F. Supp. 2d 1330 (N.D. Ga. 2005), appears at JA 194-242; see also Pet. App. 24a-72a.

JURISDICTION

The order and judgment of the Court of Appeals was entered on December 19, 2006, JA 244; Pet. App. 1a, and rehearing was denied on February 12, 2007, Pet. App. 73a. This Court granted the petition for writ of certiorari on May 29, 2007. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTES OR OTHER PROVISIONS INVOLVED

Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act" or "the Act"), 49 U.S.C. § 11501 (2002), is set forth in the Pet. App. at 75a-77a.[1]

STATEMENT OF THE CASE

Redressing decades of damaging state and local tax discrimination against interstate railroads, Congress in 1976 empowered federal district courts to enjoin the collection of property tax when the ratio of assessed value to the "true market value" of railroad property exceeds the same ratio for other commercial and industrial property in the State by 5%

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[1] There are some differences in language between Section 306 as originally enacted in § 306 of Pub. L. No. 94-210, 90 Stat. 31, 54-55 (1976), and as subsequently codified at 49 U.S.C. § 11503 (which was later redesignated as 49 U.S.C. § 11501). The recodification, however, was not intended to effect any substantive change. *Burlington N. R.R.* v. *Okla. Tax Comm'n*, 481 U.S. 454, 457 n.1 (1987).

or more. 49 U.S.C. § 11501(b)(1) & (c). The 4-R Act thus defines a precise formula for proving discrimination based on the economic standard of true market value. The plain meaning of this language is to require the district court to make an independent finding of the "*true* market value" of railroad transportation property. The determination of value is a question of fact that courts routinely decide based on evidence at trial.

Improperly invoking the federalism-based "clear-statement" canon of *Gregory* v. *Ashcroft*, 501 U.S. 452 (1991), to rewrite the statute, the Eleventh Circuit held categorically that "railroads may not challenge state valuation methodologies under subsection (b)(1)." JA 257; see JA 260 (defining valuation methodology to encompass "all nonfactual determinations . . . [of the State's appraiser] in constructing a valuation process, regardless of how broad or narrow they may be"). The court below thus upheld the exclusion of CSXT's expert testimony on the market value of its property. The Eleventh Circuit's exclusionary rule not only finds no support in the statute, but also makes the non-discrimination provisions completely hollow. A district court's independent determination of a property's market value in adjudicating a federal discrimination claim does not trench upon the State's sovereign power to tax. Because the valuation approaches at issue here are simply standard appraisal tools to generate evidence of a given property's value, a district court must be free to receive competing expert testimony on market value to resolve this factual element of a federal discrimination claim. Most fundamentally, the Eleventh Circuit's rule immunizes a principal means by which States practice discrimination, namely, the adoption and weighting of valuation methods that yield inflated estimates of the market value of railroad property. This Court should not interpret this remedial antidiscrimination statute to be self-defeating, and therefore should reverse the judgment below.

A. Statutory Background

1. Nearly 50 years ago, Congress began an exhaustive examination of the economic situation of the railroad industry in what has since become known as the "Doyle Report." S. Rep. No. 87-445 (1961). The Report identified "trends which g[a]ve cause for concern for the future overall adequacy and efficiency of our transportation system and for the health if not the very existence of common carriers." *Id.* at 47. The Report recognized that "the chief tax burden on railroads is applied by State and local governments," *id.* at 567, and identified "a studied and deliberate practice of assessing railroad property as a proportion of full value substantially higher than other property." *Id.* at 458.

The Doyle Report spurred Congress to hold a series of hearings to consider legislation addressing state-tax discrimination against railroads. On the basis of those hearings, Congress determined that interstate railroads "are easy prey for State and local tax assessors" and that "'the existence of inequitable State and local property assessments and tax policies has served to jeopardize the continued existence of essential rail passenger service.'" S. Rep. No. 91-630, at 2-3 (1969). For example, a 1968 Committee Report highlighted that "[i]n the last 7 years, the railroads alone have been assessed more than $800 million in discriminatory taxes." S. Rep. No. 90-1483, at 2 (1968). In 1972, Congress found that the 19 States that imposed the greatest excess tax burden on railroads on average overtaxed railroads relative to other property in the State by almost 40 percent. S. Rep. No. 91-630, at 5-6 & tbl. In 1975, Congress found that because of discriminatory state taxation, "railroads are over-taxed by at least $50 million each year." H.R. Rep. No. 94-725, at 78 (1975). Congress concluded that discrimination contributed to the "extremely bleak" economic state of the railroad industry. *Id.* at 80.

Congress also recognized that protections for railroads were limited absent remedial federal legislation. Although some federal and state courts had "voided discriminatory tax as-

sessments and levies on common carrier property" based on express state-law protections, those decisions did "not reach the situation . . . where the express provisions of State law or a State constitution permit such discriminatory treatment." S. Rep. No. 90-1483, at 6-7. Moreover, federal constitutional challenges provided little relief. See *id.* at 7. States were permitted to classify carrier property in a separate class from other taxable property in the same district. See *Nashville, Chattanooga & St. Louis Ry.* v. *Browning*, 310 U.S. 362, 368-70 (1940). Thus, it was no surprise that Congress determined that "[c]omplaints to the courts about relative discrimination . . . are seldom successful." S. Rep. No. 87-445, at 454; see also *id.* at 471 ("[T]here was much reason to accept the observation of one writer on constitutional law that 'States can tax interstate commerce if they go about it the right way.'") (footnote omitted). Accordingly, Congress concluded "that such discrimination must be ended." S. Rep. No. 92-1085, at 7 (1972).

2. Finally, in 1976, after eight major railroad bankruptcies, Congress enacted the 4-R Act to address the myriad problems that had been caused by the then-current state of the law. H.R. Rep. No. 94-725, at 53; S. Rep. No. 94-499, at 2-3 (1975). Section 306 was a critical part of that reform, through which Congress intended "'to put an end to the widespread practice of treating for tax purposes the property of [railroads] on a different basis than other property in the same taxing district.'" S. Rep. No. 91-630, at 2.[2] Congress intended its legislation to "provide a plain, speedy, and effective remedy" in instances of discriminatory tax assessment, S. Rep. No. 90-1483, at 7, that would ensure "a safe, viable, and efficient rail industry" and promote "the national interest and the national

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[2] *See also* S. Rep. No. 91-630, at 17 ("[I]t is well recognized that the basic purpose of this legislation is to provide a solution to a longstanding and deeply rooted problem, the practice of many State or local governments['] taxing authorities setting inequitable and discriminatory assessments and tax levels on the property of the Nation's railroads.").

defense." H.R. Rep. No. 94-725, at 101; see also H.R. Conf. Rep. No. 94-768, at 1 (1975).

Section 306 of the 4-R Act (hereinafter referred to as Section 11501, its present section within the U.S. Code) specifically outlaws four enumerated taxation practices of "a State, subdivision of a State, or authority acting for a State or subdivision of a State" that "unreasonably burden and discriminate against interstate commerce." 49 U.S.C. § 11501(b). The first outlawed practice, at issue here, concerns States'

> [a]ssess[ing] rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.

Id. § 11501(b)(1).

States are also prohibited from "[l]evy[ing] or collect[ing] on an assessment" that is prohibited by subsection (b)(1), *id.* § 11501(b)(2), as well as from "[l]evy[ing] or collect[ing] an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction," *id.* § 11501(b)(3). Finally, States may not "[i]mpose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the Board under this part." *Id.* § 11501(b)(4).

Congress established that "[t]he burden of proof in determining assessed value and true market value is governed by State law." *Id.* § 11501(c). Finally, "notwithstanding" the Tax Injunction Act (28 U.S.C. § 1341) or the amount in controversy, Congress granted federal district courts, "jurisdiction, concurrent with other jurisdiction of courts of the United States and the States, to prevent a violation of [Section 11501(b)]." 49 U.S.C. § 11501(c). Relief could only be granted, however, "if the ratio of assessed value to true mar-

ket value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." *Id.*

Thus, Congress established a precise formula for determining when a district court could grant relief for a violation of subsection (b)(1):

$$\frac{\text{Assessed Value of Rail Transportation Property}}{\text{True Market Value of Rail Transportation Property}} \text{ exceeds by greater than 5\% } \frac{\text{Assessed Value of Other Commercial \& Industrial Property}}{\text{True Market Value of Other Commercial \& Industrial Property}}$$

B. Valuation of Property

Congress explained that "'true market value'" is the "standard to which values that have already been determined must be compared," and defined it as "the generally accepted standard for assessment purposes." S. Rep. No. 91-630, app. A at 26; S. Rep. 90-1483, app. B at 22 (same). Congress's use of "true market value" as the appropriate measure for the taxation of rail property adopted a concept widely used in the ad valorem taxation of property. *Cleveland, Cincinnati, Chi. & St. Louis Ry.* v. *Backus*, 154 U.S. 439, 447 (1894) ("the rule of all property taxation is the rule of value"). The assessment of ad valorem taxes on real or personal property generally involves three steps. First, the taxing authority calculates a market value for the subject property. See *Property Appraisal and Assessment Administration* 18 (Joseph K. Eckert ed., 1990) (hereafter "*Property Appraisal*"). Second, an "as-

sessed value" is calculated. See *id.* at 18-19. In some states the assessed value is equal to the market value; in others assessed value is a specified percentage of the market value. See Appraisal Institute, *The Appraisal of Real Estate* 29 (12th ed. 2001). Finally, the taxing authority applies a particular tax rate to the assessed value of the property.[3] See *Property Appraisal* 19. In every jurisdiction assessing an ad valorem tax, therefore, the market value of the subject property directly affects the total amount of the tax.

The "market value" of a property is the most probable price at which a willing buyer and a willing seller would agree to exchange the property in a competitive market. Appraisal Institute, *supra*, at 22; *Property Appraisal* 35 ("Generally, market value is the cash price a property would bring in a competitive and open market."); Nat'l Ass'n of Tax Admin'rs, *Appraisal of Railroad and Other Public Utility Property for Ad Valorem Tax Purposes* 2 (1954) (hereafter "*NATA Report*"); accord *United States* v. *Miller*, 317 U.S. 369, 374 (1943) ("'market value' . . . denotes what 'it may fairly be believed that a purchaser in fair market conditions would have given'" (quoting *New York* v. *Sage*, 239 U.S. 57, 61 (1915)). Market value is an objective test of value. The market value is not the value that a particular person might subjectively place on a property; it is the value that an objectively reasonable willing buyer and willing seller would reach. See *Property Appraisal* 80.

The market value of a railroad's property can be determined in two ways. The first, the summation method, individually values each tract of property in a State and then adds the resulting values to derive a total value for the taxing jurisdiction. See S. Rep. No. 87-445, at 453. The unit method, on the other hand, seeks to determine a single system-wide value for the railroad, and then to assign a portion of that system-

[3] Where a property spans more than one taxing jurisdiction (such as a property in more than one county), a fourth step is necessary: allocating the value of the property among the jurisdictions in which it is located.

wide value to the particular State (for interstate railroads) and to the individual taxing districts within the State. This allocation of value is typically proportional to the percentage of a railroad's property located within a State, often measured by factors such as track mileage. Alfred A. Ring & James H. Boykin, *The Valuation of Real Estate* 428-29 (3d ed. 1986). The unit method has been recognized to be a superior method of valuing railroads, largely because it allows a more ready consideration of the railroad's going concern value. See *id.* at 419 ("Railroads . . . are more than a summation of lumber, steel, brick, and mortar. They are going concerns that succeed or fail as a 'whole.'"); *NATA Report* 2 (unit appraisal of utilities is "markedly superior" than summation method). Almost all States, including Georgia, that apply a property tax to railroads use the unit method. See N.Y. State Office of Real Prop. Servs., *Survey of Railroad and Utility Taxation Practices Among the States* tbl.1, *available at* http://www.orps.state.ny.us/ref/pubs/railroadutility/section1.htm (last modified May 17, 2005); James F. Runke & Alan E. Finder, *State Taxation of Railroads and Tax Relief Programs* 27 (1977).[4]

The market value of a property at a given point in time "is not a matter of arithmetical calculation and is not governed by any fixed and definite rule." *Rowley* v. *Chicago & Nw. Ry.*, 293 U.S. 102, 109 (1934), *amended by* 293 U.S. 532 (1934).[5] Instead, ascertaining true market value for any property requires the exercise of judgment, taking into account all the

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[4] This Court has long approved of the unit method of valuing railroads. *See, e.g., Norfolk & W. Ry.* v. *Mo. State Tax Comm'n*, 390 U.S. 317, 324 (1968) ("value may be ascertained by reference to the total system of which the intrastate assets are a part"); *Louisville & Nashville R.R.* v. *Greene*, 244 U.S. 522, 548 (1917).

[5] *See Rowley*, 293 U.S. at 109 ("Facts of great variety and number, estimates that are exact and those that are approximations, forecasts based on probabilities and contingencies have bearing and properly may be taken into account to guide judgment in determining what is the money equivalent—the actual value—of the property.").

pertinent factors that influence market value. See Appraisal Inst., *supra*, at 65; *NATA Report* 8-9, 60. The professional discipline of property appraisal has developed a variety of techniques to aid property appraisers in assessing the value of property. Appraisers generally study property from three different viewpoints, referred to as the "approaches" to value. Appraisal Inst., *supra*, at 62. These approaches are the cost approach, the sales comparison approach, and the income capitalization approach. See *id.* at 62-65; JA 246; JA 63-64; S. Rep. No. 87-445, at 455-56, 475-78.

The cost approach is predicated on the assumption that a property's value is related to its cost. See Appraisal Inst., *supra*, at 63. Under the cost approach, the estimated value of the land is added to the estimated cost of reproducing all buildings and improvements on the land, minus the amount of depreciation in the structures. See *id.* The cost approach is not well suited for properties with older structures with substantial depreciation, because of the difficulty in accurately estimating obsolescence. See *id.* at 62; *NATA Report* 8.

The sales comparison approach is most useful for properties that are frequently exchanged on the market, such as single-family homes. See Appraisal Inst., *supra*, at 63-64. An appraiser using the sales comparison approach will identify properties sold in the subject property's market that have similar characteristics. See *id.* From these comparable sales, the appraiser derives an indicated value for the subject property. See *id.* Because it is predicated on actual market transactions, the sales comparison approach is a strong indicator of value where there is sufficient sales data to support it. See *id.* at 63; JA 64. It has little utility, however, for properties that are rarely sold on the open market. See Appraisal Inst., *supra*, at 62.

A variant of the sales comparison approach, known as the stock-and-debt approach, has emerged for publicly traded corporations that involve interstate networks (such as railroads and utilities). Because the enterprise as a whole is rarely sold,

and thus there is "seldom available objective market evidence as to the price that railroads or public utilities would command if offered for sale, the next best alternative is the market price of the stocks and bonds of the enterprise owning the property." Ring & Boykin, *supra*, at 426. Although theoretically sound for an enterprise comprised solely of assets subject to assessment, the stock-and-debt valuation approach in practice yields "dubious and unreliable evidence of the value of the assets that are subject to assessment for ad valorem purposes." *Id.* The reason is that many enterprises own assets that are not subject to assessment for property taxes (such as shares of subsidiaries or investments). Furthermore, given the many factors (such as interest rates) that affect stock and bond prices, "[t]here is no reliable relationship between the constantly fluctuating market of stocks and bonds and the tangible and intangible assets reflected by such securities." *Id.* Appraisers generally do not use this approach to determine value, but "appraisal practice does sanction this method as a possible check on the reasonableness of the final estimate of value." *Id.*

The third approach, the income approach, assumes that a property's value is equivalent to its earnings potential. See *id.* at 64; Roger A. Morin, *Regulatory Finance: Utilities' Cost of Capital* 99 (1994) ("the value of an asset stems from the discounted present value of its future cash flow stream"); *Monongahela Navigation Co.* v. *United States*, 148 U.S. 312, 328 (1893) ("The value of property, generally speaking, is determined by its productiveness—the profits which its use brings to the owner."). This approach therefore estimates the present value of a property's future earnings. See Appraisal Inst., *supra*, at 64. An appraiser using the income approach must both determine the likely future income stream and discount future earnings to present value. See *id.* at 64-65.

Each of these three general approaches encompasses several specific analytical techniques. See *id.* at 50. For instance, an appraiser seeking to estimate value through an in-

come capitalization approach could do so through a direct capitalization analysis, a yield capitalization analysis, or a discounted-cash-flow analysis, each of which has various permutations which "yield value conclusions that differ importantly from one another." Ring & Boykin, *supra*, at 333.

Appraisers ordinarily select and apply several valuation methodologies, so that the results of the methodologies can be used as a check on the others. See JA 79; Appraisal Inst., *supra*, at 62. The selection of methodologies must be made in light of the data and the appraiser's professional judgment. See *id.* Appraisers are to "consider[] all conceptual approaches deemed to be relevant by the appraiser," and to "select and apply appropriate valuation approaches, methods, and procedures." Am. Soc'y of Appraisers, *Business Valuation Standards* 5, 6 (2002). The determination of which valuation techniques are appropriate depends on factors such as the characteristics of the property, the available data, and the appraiser's own professional opinion of the utility of the various techniques. See Appraisal Inst., *supra*, at 50, 62; S. Rep. No. 87-445, at 452 ("Valuation or appraisal is a *process* by which an assessor arrives at his *opinion* of the value of the property") (emphasis added). Ultimately, the choice of techniques "depends on the judgment of the appraiser and not on any prescribed formula." Am. Soc'y of Appraisers, *supra*, at 14; see also William N. Kinnard, Jr., *Income Property Valuation: Principles and Techniques of Appraising Income-Producing Real Estate* 49 (1971).

Once methodologies have been selected and applied to the subject property, the appraiser must arrive at his or her opinion of value. No one methodology of value produces the "true market value" of the property. Instead, the different value approaches, and the valuation methodologies within the approaches, are "evidence of value," which the appraiser should consider in exercising his or her professional judgment to arrive at an opinion of value. *NATA Report* at 8; see *id.* at 60 (none of "the value evidences" are "sufficiently error-

proof to warrant implicit reliance" on any single evidence or formulaic average of evidences); JA 123. Sound appraisals therefore are based not on mechanical formulas, but rather on an appraiser's consideration of the different evidence of value in light of "common sense, informed judgment and reasonableness." Rev. Rul. 59-60, 1959-1 C.B. 237 § 3.01.

In general, appraisers give the most weight to the methodology that is most supportable in light of the available data. See *Property Appraisal* 108. If different evidence of value suggests widely different results, appraisers often will use their judgment to discount the methodologies that are less reliable. See *NATA Report* at 8 ("[W]hen one evidence of value varies widely from the others, it should be a warning signal to examine critically the underlying data to see whether this evidence is really persuasive in this particular case. If it is not, this evidence of value should be ignored, or at best should weigh very lightly in the decision . . . .").

While the size and unique characteristics of railroads—and particularly interstate railroads—make the valuation of railroad property more complex than the valuation of most real property, the determination of "true market value" for a railroad's property is governed by the same principles as for any property valuation. An appraiser assessing the value of railroad property chooses techniques to generate evidence of a value and should use the results of those techniques as evidence in forming his or her professional opinion as to market value. Ring & Boykin, *supra*, at 427; *NATA Report* 8, 60.

C. *Burlington Northern Railroad* v. *Oklahoma Tax Commission*

Eleven years after the 4-R Act became law, this Court determined whether section 11501(b)(1) "permits review by federal courts of alleged overvaluation of railroad property by state taxation authorities." *Burlington N. R.R.* v. *Okla. Tax Comm'n*, 481 U.S. 454, 456 (1987). Noting the congressional finding that "'railroads are over-taxed by at least $50 million

each year,'" this Court held that Congress chose to accomplish "the goal of furthering railroad financial stability" by prohibiting "discriminatory state taxation of railroad property." *Id.* at 457 (quoting H.R. Rep. No. 94-725, at 78). Section 11501 was "Congress' solution to the problem of discriminatory state taxation of railroads." *Id.*

This Court stated that "the language of [§ 11501] plainly declares the congressional purpose," for "[i]t is clear from this language that in order to compare the actual assessment ratios, it is necessary to determine what the 'true market values' are." *Id.* at 461. Therefore, the Court ruled, "assessed value and true market value are subjects for judicial inquiry," *id.* at 462. This Court found that the statute's plain meaning foreclosed a cramped construction of the term "true market value" to mean "'state determined market value'" (the reading favored by the state authorities) or state-determined market value absent proof of intent to discriminate (the reading adopted by the court of appeals). *Id.* at 461-63. Accordingly, the Court dismissed concerns about federalism, burdens on federal courts, and state tax collection delays, stating:

> These are policy considerations which may have weighed heavily with legislators who considered the Act and its predecessors. It should go without saying that we are not free to reconsider them now.

Id. at 464.

In passing, this Court briefly explained in a footnote an issue that had not been presented by petitioner and left that issue open for resolution another day:

> Petitioner has not challenged the valuation methodology employed by respondents in determining the value of petitioner's railroad; petitioner's sole challenge is to the application of that methodology . . . . This case therefore does not present the question whether a railroad may, in an action under [Section 11501] challenge in the district court the appropriateness of the accounting

> methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied. Accordingly, we express no view on that issue.

Id. at 463 n.5. This case brings the Court to that other day.

D. Factual Background

This case involves CSXT's challenge to the 2002 assessment of its property by the State Board of Equalization of Georgia ("the Board"), and raises the issue left open in *Oklahoma Tax*. Under Georgia law, most commercial and industrial property is locally assessed by county boards, but public utilities (including railroads) are centrally assessed by the State. Georgia counties are permitted, but not required, to use the State's proposed assessment in imposing taxes. JA 245-246.

In Georgia, the Property Tax Division of the Georgia Department of Revenue ("the Department") has traditionally valued railroad transportation property by use of the unit method, although there are no state constitutional, statutory, or regulatory provisions dictating the methodology the Department must use. In 2002, Gregg Dickerson, a program manager, performed the appraisal. JA 201. Mr. Dickerson changed the approaches and techniques used to calculate unit value. Formerly, railroad transportation property was valued using a yield capitalization method (an income approach), a direct capitalization method (an income approach), and a stock-and-debt method (a sales comparison approach). For the 2002 tax year, Mr. Dickerson replaced the first two of those methods with a discounted cash flow ("DCF") method (an income approach) and a market multiples method (a sales comparison approach). JA 247.

Mr. Dickerson generated five values from these approaches, ranging from $8.126 billion (using the DCF method) to $12.346 billion (using the market multiples

method). JA 247-248. Mr. Dickerson selected a unit value of $8.2 billion as close to the lowest of his estimates.[6] JA 248. Mr. Dickerson's 2002 overall unit value for CSXT of $8.2 billion was 47% higher than the 2001 valuation. JA 232. After adjustments and deductions, Mr. Dickerson calculated taxable market value of CSXT's property in Georgia (based on the percentage of rail miles in the State) at $514.9 million. JA 248. That was an increase of 36% from the 2001 Georgia taxable value of CSXT's property. Moreover, in 2002, CSXT's property tax liability in Georgia was $6.5 million, whereas its 2001 liability was only $4.6 million. It was undisputed below that no major non-railroad utility taxpayer received any significant increases in values between 2001 and 2002. JA 151.

E. Proceedings Below

1. *The District Court.* CSXT filed a complaint in the United States District Court for the Northern District of Georgia challenging the Department's valuation under Section 11501(b)(1) of the 4-R Act. JA 248. In this case, the ratio of the assessed value to the true market value of other commercial and industrial property was not disputed. Thus, in order to determine whether the assessed value of CSXT's property as determined by Mr. Dickerson was discriminatory, the pivotal issue was what was the true market value of CSXT's property.

After CSXT filed suit, Mr. Dickerson prepared "a complete appraisal of CSXT using essentially the same three valuation methods that he [had] employed" earlier. JA 203. However, after discovery, Mr. Dickerson prepared "a revised full appraisal of CSXT" in which he changed "the calculation of the cost of equity used in deriving the weighted cost of capital." *Id.* As a result of this change, Mr. Dickerson "ultimately

[6] While Mr. Dickerson stated that $8.2 billion was at the bottom of the range of unit values for CSXT, JA 202, his estimate was the highest among the 15 States where CSXT operates that use the unit value method, JA 169.

opined that the fair market unit value of CSXT was $11.807 billion." JA 204.

CSXT argued and proved that its true market value was $6 billion, and thus the State had violated Section 11501(b)(1), since CSXT "was taxed at a higher ratio of assessed value to true market value than other commercial and industrial property." JA 249-250. CSXT submitted an appraisal prepared by a valuation expert, Thomas Tegarden, whose credentials were described by the district court as "'impeccable.'" JA 250 (quoting JA 195).[7] Mr. Tegarden used three different approaches to approximate "true market value," but relied primarily on a yield capitalization analysis. JA 250. Based on a unit value of $6 billion, he calculated the value of CSXT's Georgia property as worth $369.3 million. JA 194.

Thus, CSXT was taxed as though the unit value of its property was worth $8.2 billion, when based on Mr. Tegarden's analysis, the unit value of its property was worth only $6 billion. The parties agreed that the other commercial and industrial properties in the State were taxed at their true market value. Because Mr. Tegarden's appraisal indicated that CSXT's property was appraised for assessment purposes at a value that was 137% of its true market value, unlike other commercial and industrial properties, which were appraised

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[7] The district court correctly assessed Mr. Tegarden's credentials. Among other appraisal designations, he is both a Member of the Appraisal Institute, which is considered "the highest appraisal designation offered in the field of appraisal," and a Certified Assessment Evaluator of the International Association of Assessing Officers, which is "the highest designation offered by that organization." JA 128; JA 164. He has more than 35 years of appraisal and consulting experience on behalf of taxpayers and numerous state and local revenue departments, including the Georgia Department of Revenue. JA 164-165. He also has 15 years experience with the Tennessee Public Service Commission, which at the time was responsible for the "tax valuation of public utilities and railroads." JA 166. In contrast, Mr. Dickerson holds no appraisal designation from the Appraisal Institute and has never done a "formal written unit rule appraisal" before this case. JA 149-150.

for assessment purposes at 100% of their true market values, CSXT argued that the State had discriminated against CSXT.

The district court held that it was not permitted to consider Mr. Tegarden's appraisal because the 4-R Act barred consideration of appraisals "based on a valuation methodology different from the methodology used by the State, unless the methodology of the State is irrational or intentionally discriminatory." JA 250. The district court elaborated:

> This is a case brought under the 4-R Act and the court must determine the true market value of CSXT. *CSXT, in turn, has the burden of proving by a preponderance of the evidence that the true market value of its property is $6 billion.* To do this, CSXT presented two types of evidence. First, it criticized the Department's calculations. Second, it presented a valuation of its property by Mr. Tegarden. *In a more typical case, the court would look to both Mr. Tegarden's appraisal and the Department's appraisal to determine the true market value of CSXT.* If the court found by a preponderance of the evidence that CSXT's true market value was $6 billion, as proposed by CSXT, then the court would compare the Department's Proposed Valuation to CSXT's true market value to determine if discrimination occurred. *However, as explained later in this order, the court cannot consider Mr. Tegarden's valuation because it was prepared using different valuation methods than the Department. The court, therefore, is limited to looking solely at CSXT's criticisms of the Department's valuation.*

JA 207 n.8 (emphases added).

The district court further rejected CSXT's argument that Mr. Tegarden's valuation methodology was a variant of the State's own methodology. JA 215. Finally, the district court rejected CSXT's challenges to the Board's calculations, and, using Mr. Dickerson's discounted cash flow number with

some modifications, found that the unit value of CSXT's property was $7.7 billion. JA 241 & n.32. The court therefore found that the ratio of assessed to market value of CSXT's property did not exceed by more than 5% the same ratio for other commercial and industrial property, and entered judgment for the Board. JA 241-42.

2. *The Eleventh Circuit.* A divided court of appeals affirmed. The court began by stating that "[w]hether a railroad may challenge, under the 4-R Act, the valuation methodology of a state is a question the Supreme Court has acknowledged but not decided." JA 252 (citing *Okla. Tax*, 481 U.S. at 462-63 & n.5). The Eleventh Circuit employed a clear statement canon as necessary to uphold the State's approach. The court relied upon this Court's decision in *Department of Revenue* v. *ACF Industries, Inc.*, 510 U.S. 332 (1994), a case which involved a different subsection of Section 11501. JA 256-57. The court below found no clear statement that federal courts could determine true market value using methodologies other than those of state assessors: "[R]ailroads may not challenge state valuation methodologies under subsection (b)(1). The text of the Act does not clearly state that railroads may challenge valuation methodologies. Without that clear statement of congressional intent, the argument of the Railroad fails." JA 257. The district court, it concluded, had to accept "all nonfactual determinations . . . [of the state appraiser] in constructing a valuation process, regardless of how broad or narrow they may be," including not only his choice of analytical techniques but the weighting of the results of those analyses. JA 259-260.

Judge Fay dissented with regard to this holding. JA 263. Judge Fay declared that "[t]he language of the statute is straightforward and prohibits states from assessing rail transportation property at a value that has a higher ratio to the true market value than the ratio that the assessed value of other commercial and industrial property has to its true market value." *Id.* Judge Fay concluded:

> Since the objective of any methodology is a determination of *true market value*, a railroad should be allowed to challenge the method used in an attempt to prove that the result of such a method was not the *true market value* of its property. . . . If the Railroad can prove that the method used by the state does not result in a fair appraisal of true market value and that the assessed value is in fact at a ratio higher than five percent of the ratio of true market value and assessed value of other commercial and industrial property, it is entitled to relief.

JA 266.

SUMMARY OF ARGUMENT

The Eleventh Circuit held that the 4-R Act's grant of power to a federal district court to determine the "true market value" of railroad transportation property in assessing tax discrimination by state governments is limited to finding error in the state appraiser's "factual determinations" in applying valuation techniques. According to the Eleventh Circuit, the statute forbids a district court, in determining true market value, to consider the railroad's expert testimony on market value (or otherwise consider any evidence of value) based on valuation techniques not used by the State's appraiser.

The Eleventh Circuit's exclusionary rule has no foundation in the statute, and is inimical to a statute designed to remedy tax discrimination by state and local authorities. Section 11501(b)(1) prescribes a precise formula for measuring discrimination. Under that formula, true market value is the economic standard by which the existence and degree of discrimination is determined. The market value of a property, and the choice and weight assigned to various techniques for estimating value, are questions of fact, and valuations of property using the techniques at issue here "are routinely made in judicial proceedings." *Suitum* v. *Tahoe Reg'l Planning Agency*, 520 U.S. 725, 741-42 (1997).

Congress did not require proof of "true market value" as an element of a section (b)(1) discrimination claim, but deprive railroads of the power of proving that element with independent valuation evidence. The Eleventh Circuit's characterization of the state appraiser's choice to compare and weigh particular income capitalization and sales comparison techniques as "delicate matters of state policy," JA 260, is unfounded. In any property valuation, it is the standard practice of professional appraisers to employ multiple techniques to generate different evidence of value, which the appraiser considers in reaching a final judgment of value, based on the nature of the property, the relative reliability of the different techniques, and the soundness of the data. Such choices do not involve policymaking. Thus, the plain and ordinary meaning of Congress's delegation to federal courts to determine the "true market value" of railroad transportation property is to make an independent determination of market value, based on any relevant evidence of value presented by the parties.

Nothing in the Act restricts the district court to considering only that evidence of value generated by techniques favored by the state appraiser. The district court does not review the State's methodology for discriminatory purpose or arbitrariness; it does not examine whether States use the same or different valuation methods for railroad and commercial and industrial property; and even if it finds a violation, it does not enjoin the State from using any particular valuation method or technique in future valuations and assessments. Instead, Congress has defined discrimination solely in terms of a comparison of the ratios for assessed-to-true market value of railroad transportation property versus other commercial and industrial property. The district court (1) makes findings of fact on the assessed and true market value of each kind of property, (2) compares the ratios, and (3) may grant relief as long as the railroad ratio is at least 5% higher than the ratio for other commercial and industrial property. 49 U.S.C. § 11501(b)(1) & (c). Claims of contrary "state valuation pol-

icy" cannot prevent an independent judicial finding according to the precise standards of the 4-R Act of whether the State has discriminated against the railroad in valuing and assessing property for tax purposes.

Indeed, the district court's statutory duty to determine "*true* market value" precludes the Eleventh Circuit's construction, which enjoins the district court to accept the methods, approaches, and techniques used by the States even if the valuation results they produce are *inaccurate* and *unreliable*. Other provisions of the statute confirm that the district court is to make an independent determination of market value in adjudicating (b)(1) discrimination claims. Indeed, the Eleventh Circuit's construction disregards the context in which the 4-R Act was passed. As documented in congressional studies and hearings, the valuation methods and practices that the States employed were a major source of discrimination against the railroads. See *infra*, at 35-36, 38. Those methods and practices included using flawed valuation approaches (such as reproduction cost) that inflated railroad valuations, or requiring more frequent revaluations of railroad property that caused assessments to increase more rapidly than other property assessments. Congress did not pass a self-defeating statute that grants a discrimination remedy in district court, but disables courts from rectifying one of the principal means by which states discriminate against railroads.

The Eleventh Circuit's reliance on the clear-statement canon of *Gregory* v. *Ashcroft* is misplaced. That canon applies only when there are two permissible constructions of an ambiguous statute. Even the Eleventh Circuit did not suggest that (absent federalism concerns) the term "true market value" can be plausibly interpreted to mean the state appraiser's valuation of the property, adjusted for mere arithmetic errors. The Eleventh Circuit's exclusionary rule is simply an implied limitation on the railroad's proof to vindicate putative state interests. But the *Gregory* canon does not license the judiciary to rewrite the statute. In any event, the natural meaning

of subsection (b)(1) – that a court may consider any relevant evidence of value in defining "true market value" of property for the sole purpose of deciding a discrimination claim – does not alter the constitutional balance between state and federal governments. Congress altered that balance by imposing a federal prohibition on discrimination practices that were prevalent in the States. No constitutional question is avoided by a statutory construction that limits the evidence the district may receive in adjudicating a subsection (b)(1) claim.

Department of Revenue v. *ACF Industries, Inc.*, 510 U.S. 332 (1994), relied on by the Eleventh Circuit, is not to the contrary. That case concerned a different part of the 4-R Act (subsection (b)(4)). The construction of subsection (b)(4) proposed by the plaintiffs – abolition of state power to grant legislative exemptions for certain kinds of commercial property from ad valorem taxation – would have constituted a significant invasion of state sovereignty. The Court there did not apply the *Gregory* canon to resolve ambiguity; rather it determined that the statute, construed as a whole, had a more limited meaning, and that principles of federalism prohibited expanding its preemptive force beyond its "evident scope." *Id.* at 345. The *ACF* Court specifically contrasted (b)(4) with (b)(1) – the statute at issue here – construing the latter to declare "*precise standards for judicial scrutiny of challenged rate and assessment practices.*" *Id.* at 343 (emphasis added). Nothing in *ACF* supports rewriting (b)(1), so that it defeats the purpose for which Congress enacted the 4-R Act.

Finally, recourse to the legislative history is unnecessary given the plain meaning of subsection (b)(1), but that history simply shows that even the opponents of the Act understood that district courts would make independent determinations of true market value.

The 4-R Act is an antidiscrimination statute meant to protect railroads from the damaging effects of unfair and excessive property taxation. The Eleventh Circuit's exclusionary rule is irreconcilable with the plain text and purpose of the

statute, and should be rejected. CSXT was taxed as though the unit value of its property was worth $8.2 billion, when, based on the expert testimony of Mr. Tegarden, the unit value of its property was worth only $6 billion. CSXT should be given an unrestricted opportunity to introduce such evidence of value, and thus to show that its property was discriminatorily appraised for assessment purposes at a value that was 137% of its true market value, unlike other commercial and industrial properties, which were appraised for assessment purposes at 100% of their true market values.

ARGUMENT

I. THE PLAIN LANGUAGE OF THE ACT REQUIRES FEDERAL COURTS TO DETERMINE TRUE MARKET VALUE AND PERMITS THE RAILROAD TO CHALLENGE THE VALUATION METHODS USED BY THE STATE'S APPRAISER.

The Eleventh Circuit improperly held that federal courts must use the methodologies of the state assessors in determining the true market value of railroad property. The Eleventh Circuit's rule is contrary to the language, history, and purpose of § 11501. A federal court cannot accomplish its statutory mandate of determining the ultimate fact of "*true* market value" if it is hamstrung by the Eleventh Circuit's rule that the reviewing court must accept the state assessor's valuation methods. As Judge Fay logically explained in his dissent below, "[s]ince the objective of any methodology is a determination of *true market value*, a railroad should be allowed to challenge the method used in an attempt to prove that the result of such a method was not the *true market value* of its property." JA 266.

"The starting point for [the] interpretation of a statute is always its language," *Cmty. for Creative Non-Violence* v. *Reid*, 490 U.S. 730, 739 (1989), and "courts must presume that a legislature says in a statute what it means and means in a statute what it says there," *Conn. Nat'l Bank* v. *Germain*, 503

U.S. 249, 253-54 (1992). Where, as here, the words of the statute are unambiguous, the "'judicial inquiry is complete.'" *Id.* at 254. The Eleventh Circuit's myopic interpretation of Section 11501(b)(1) cannot be reconciled with the plain language of the statute.

Here, Congress has charged the federal district courts with the duty to determine whether state or local authorities are discriminating against railroads by assessing railroad property at a higher ratio to "true market value" than the ratio of assessed to "true market value" of other commercial and industrial property. 49 U.S.C. § 11501(b)(1). The term "*true* market value" precludes any deference to a state or local tax authority as to what the market value is; Congress clearly intended the district court to make an independent finding on this element of a discrimination claim.

Indeed, in *Oklahoma Tax*, this Court rejected the claim of a state tax authority that the statutory term "true market value" should be construed as "'state determined market value.'" 481 U.S. at 461. Dismissing the State's arguments premised on the legislative history, comity, and imputed congressional intent, this Court held:

> In the present case, *the language of [§ 11501] plainly declares the congressional purpose*. Subsection (b)(1) forbids any State to "assess rail transportation property at a value that has a higher ratio to the true market value . . . than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property." *It is clear from this language that in order to compare the actual assessment ratios, it is necessary to determine what the "true market values" are.*

Id. (emphases added) (omission in original). This Court refused to adopt a position that "depends upon the addition of words to a statutory provision which is complete as it stands.

Adoption of [such a] view would require amendment rather than construction of the statute, and it must be rejected here." *Id.* at 463.

To be sure, *Oklahoma Tax* did not express any view on "whether a railroad may, in an action under [§ 11501], challenge in the district court the appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied." *Id.* at 463 n.5. As the Court noted, that issue was not presented. Burlington Northern challenged only the application of the State's chosen methodology, "particularly the State's evaluation of the cost of capital and the State's refusal to make deductions for property which petitioner claims is obsolete." *Id.* But the plain language of the statute and the logic of *Oklahoma Tax* compel the same result here. By committing the determination of the ultimate fact of "true market value" to the courts in a section 11501(b)(1) action, Congress necessarily intended that the district court would decide that question of fact based on all relevant evidence. Nothing in the statute compels exclusion of the railroad's expert testimony on different evidence of value yielded by reliable valuation approaches that the state appraiser ignored.

A. The Plain Meaning Of Section 11501(b)(1) Is That "The True Market Value Of The Rail Transportation Property" Is A Question Of Fact Committed To The Court Without A Restriction On The Probative Evidence The District Court May Consider.

As this Court recognized in *Suitum* v. *Tahoe Regional Planning Agency*, 520 U.S. 725 (1997), even in the absence of a functioning market, the market value of property is "simply an issue of fact about possible market prices," and "determinations of market value are routinely made in judicial proceedings without the benefit of a market transaction" "in good faith and at arm's length." *Id.* at 741-42. In such cases, the

courts typically determine value on the basis of "'opinion evidence,'" *id.* at 742 (quoting 5 J. Sackman, *Nichols Law of Eminent Domain* § 23-01, at 23-6 (rev. 3d ed. 1997)), including (as here) "expert testimony relating to comparable sales and discounted cash flow." *Id.*

The distinction the Eleventh Circuit drew between "factual determinations" in valuation (for the court) and "nonfactual determinations" (reserved for the State as matters of policy) has no basis in the 4-R Act. As discussed *supra*, at 8-12, the different valuation methodologies, approaches, and techniques are simply tools to generate "evidence of value," which the appraiser considers in exercising his or her professional judgment to arrive at an opinion of value. *NATA Report* at 8; see *id.* at 60. When an appraiser renders an ultimate judgment of market value, professional standards require consideration of "all conceptual approaches deemed to be relevant." Am. Soc'y of Appraisers, *supra*, at 5. Valuation is a factual judgment specific to the property based on "the nature of the problem, the probable applicability and responsiveness of the several analytical methods employed to that problem, the adequacy and reliability of the data used in applying those analytical methods, and the logic and validity of [the appraiser's] own thought processes in conducting the analysis." Kinnard, *supra*, at 52. Congress well understood the nature of valuation in enacting the 4-R Act. See S. Rep. No. 87-445, at 452-59, 475-81; see also Am. Inst. of Real Estate Appraisers, *The Appraisal of Real Estate* 69-70 (4th ed. 1964) (valuation approaches are "indications of value" used to inform the appraiser's "judgment" to "arrive[] at a considered final estimate of value").

The plain meaning of undefined statutory language is its "ordinary meaning." *FMC Corp.* v. *Holliday*, 498 U.S. 52, 57 (1990). Subsection (b)(1) defines a precise formula for proving discrimination that is measured by true market value. A district court's finding of discrimination in violation of the 4-R Act turns upon the outcome of that formula, not upon the

particular valuation techniques that the state appraiser employed. The district court does not review the State's methodology for arbitrariness or discriminatory purpose; it is unconcerned with whether the valuation methods the State uses for railroad or commercial and industrial property are the same or different; and even if it finds a violation, the district court does not enjoin the State from using any particular valuation method or technique in future valuations and assessments. Rather, Congress has defined discrimination solely in terms of a comparison of the ratios for assessed-to-true market value of railroad transportation property and other commercial and industrial property. The district court makes findings of fact on the assessed and true market value of each kind of property; compares the ratios; and may grant relief so long as the railroad ratio is at least 5% higher than the ratio for other commercial and industrial property. 49 U.S.C. § 11501(b)(1) & (c).

The market value of railroad property has long been recognized to be a question of fact. See *Pittsburgh, Cincinnati, Chi. & St. Louis Ry.* v. *Backus*, 154 U.S. 421, 434 (1894) ("[t]he true cash value of the plaintiff's [railroad] property . . . was a question of fact"). Thus, the power vested in a court adjudicating a section 11501(b)(1) claim to render the ultimate fact determination of the "true market value" of railroad property necessarily includes the power to evaluate all relevant "evidence of value," *NATA Report* at 8, including competing expert opinion testimony applying reliable valuation methodologies, approaches, and techniques, and then weighting the results thereof.

Indeed, in a wide variety of judicial proceedings, both the market value of property and the methodologies used in determining that market value have long been recognized to be questions of fact. In eminent domain proceedings, the finder of fact makes the determinations of market value based on opinion testimony, *Suitum*, 520 U.S. at 741-42, including what "assumptions" are appropriate in making "a guess of

informed persons" as to the value of property that is not actively priced in a market. *Miller*, 317 U.S. at 374-75. Neither the value of the property nor the methodology for determining that value may be altered by legislative policy. The legislature may neither "say what compensation shall be paid" nor determine "what shall be the rule of compensation." *Monongahela Navigation*, 148 U.S. at 327. Instead, the ascertainment of the property's value and of any "rule[s]" for deriving that value are matters of fact for the court. *Id.* See *Albert Hanson Lumber Co.* v. *United States*, 261 U.S. 581, 589 (1923) (value of property taken for eminent domain was question of fact for the jury); *United States* v. *0.376 Acres of Land*, 838 F.2d 819, 827-28 (6th Cir. 1988) ("In a condemnation trial, the ultimate factual issue of determining the fair market value of any given parcel of real estate is submitted to the trier of fact, which fact finder, after having had the opportunity of assigning credibility and weighing the testimony of the expert witnesses presented by the adversary parties to the action, determines that value.").

Similarly, in federal tax cases, the Tax Court's determinations of the fair market value of property "is ultimately a finding of fact," *Palmer* v. *Commissioner*, 523 F.2d 1308, 1310 (8th Cir. 1975) (estate tax), as is its choice of an appropriate valuation methodology. See, *e.g.*, *Gross* v. *Commissioner*, 272 F.3d 333, 343 (6th Cir. 2001) ("'The choice of the appropriate valuation methodology for a particular stock is, in itself, a question of fact.'"); *Sammons* v. *Commissioner*, 838 F.2d 330, 334 (9th Cir. 1988) (choice of cost methodology to value donation was a question of fact). What is more, the Tax Court is not bound by the valuation methodologies chosen by the government; instead, it weighs all the relevant evidence and can accept the valuation evidence of the taxpayer, accept the valuation evidence of the government, or reach its own independent valuation. District courts apply the same approach in making other determinations of fair market value under the tax code:

> Complex factual inquiries such as valuation require the trial judge to evaluate a number of facts: whether an expert appraiser's experience and testimony entitle his opinion to more or less weight; whether an alleged comparable sale fairly approximates the subject property's market value; and the overall cogency of each expert's analysis. Trial courts have particularly broad discretion with respect to questions of valuation.

Ebben v. *Commissioner*, 783 F.2d 906, 909 (9th Cir. 1986) (determination of "fair market value" under federal tax laws).

The same is true for valuations in a host of other contexts, from valuing future earnings to calculate damages,[8] to valuing salvage in admiralty cases,[9] to valuing property for conversion damages.[10] Indeed, many of the techniques at issue here—such as the discounted cash flow analysis employed by the State, and the related yield capitalization analysis favored by CSXT's expert witness – are regularly presented in expert testimony as evidence for the trier of fact to consider in rendering a judgment on market value.[11] The Eleventh Circuit's

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[8] *See Monesson Sw. Ry.* v. *Morgan*, 486 U.S. 330, 342 (1988) (appropriate methodology for discounting future earnings to present value is an "essentially factual question" committed to the fact finder).

[9] *See, e.g., Margate Shipping Co.* v. *M/V JA Orgeron*, 143 F.3d 976, 990 (5th Cir. 1998) (valuation of property for salvage purposes was a question of fact; reversing because district court had chosen a valuation methodology that was not "based on principles that reflect sound reasoning"); *cf. Clark* v. *McNabb*, 878 So. 2d 677, 681 (La. Ct. App. 2004) ("the valuation method used by the trial court [for the salvage value of a vehicle] is a question of fact").

[10] *See, e.g., Cross* v. *Berg Lumber Co.*, 7 P.3d 922, 933 (Wyo. 2000) (choice between methods for conversion damages was for the trial court because "'[v]aluation of property is a question of fact, and there is no universal standard for such a determination'").

[11] *See, e.g., Energy Capital Corp.* v. *United States*, 302 F.3d 1314, 1331 (Fed. Cir. 2002) (approving use of discounted cash flow valuation of the venture in calculating lost-profits damages for breach of contract); *Kool, Mann. Coffee & Co.* v. *Coffey*, 300 F.3d 340, 362-63 (3d Cir. 2002) (up-

suggestion that the methods, approaches, and techniques for valuing railroad property are questions of state policy is inconsistent with this broad recognition that market value and the methodologies that generate evidence value are questions of fact, not matters of social policy. There is simply no basis in the statute for the exclusionary rule the Eleventh Circuit adopted to prohibit railroads from offering (and courts from hearing) an expert opinion on the value of railroad property, based on valuation approaches that differ from those used by the State's appraiser. Indeed, the absurdity of this rule is particularly acute in this case, where Mr. Tegarden is by far more qualified than Mr. Dickerson. See *supra*, at 16 n.7.

B. The Statutory Term "True Market Value" Does Not Permit The District Court Blindly To Accept The State Appraiser's Methods.

Market value "is not a matter of arithmetical calculation," *Rowley*, 293 U.S. at 109, and the necessity to use various assumptions "make it unlikely that the appraisal will reflect true value with nicety." *Miller*, 317 U.S. at 374. But Congress's charge to a district court in adjudicating a section 11501(b)(1) discrimination claim to determine the "*true* market value" of railroad property (and of commercial and industrial property), 49 U.S.C. § 11501(b)(1) (emphasis added), requires an independent and neutral finding by the district court of the market

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holding district court's reliance on discounted cash flow model to value pre-fraud business in finding fraudulent conveyance damages, despite criticism of that methodology); *Wilson* v. *Great Am. Indus., Inc.*, 979 F.2d 924, 933 (2d Cir. 1992) (approving of "capitalization of earnings method"); *In re Hotel Assocs., LLC*, 340 B.R. 554, 557-58 (Bankr. D.S.C. 2006) (considering expert testimony on yield and direct capitalization methods to value a hotel in resolving a secured creditor's claim); *Swope v. Siegel-Robert, Inc.*, 74 F. Supp. 2d 876, 887-98 (E.D. Mo. 1999) (applying yield capitalization approach in valuing minority shares of a corporation), *aff'd in part & rev'd in part*, 243 F.3d 486 (8th Cir. 2001); *In re Broad Assocs. Ltd. P'ship*, 125 B.R. 707, 713-14 (Bankr. D. Conn. 2001) (applying yield capitalization approach to value office building).

value of the property that is "true" based on the available evidence presented by the parties.

This statute cannot be reasonably read to require the district court to find the "true market value" of railroad property as an element of a federal discrimination claim, and nonetheless preclude the railroad from presenting evidence of what the "true market value" of the railroad property is. But that is exactly what the Eleventh Circuit's exclusionary rule does: it prevents the railroad from presenting its own impeccably qualified expert's opinion of true market value, arrived at by the standard (and indeed ethically required) professional practice of estimating value by considering and weighing multiple valuation techniques. Am. Soc'y of Appraisers, *supra*, at 5-6. See JA 207 n.8 ("[T]he court cannot consider Mr. Tegarden's valuation because it was prepared using different valuation methods than the Department. The court, therefore, is limited to looking solely at CSXT's criticisms of the Department's valuation.").

Indeed, the statutory requirement that the district court find "*true* market value" affirmatively forbids the Eleventh Circuit's exclusionary rule. The Eleventh Circuit immunizes the state appraiser's choice and weighting of valuation methods, approaches, and techniques from judicial inquiry, JA 258-260, and therefore the district court is forced to accept such methods, approaches, and techniques even if the valuation results they produce are demonstrably *inaccurate* and *unreliable*.

The reason that so many valuation methodologies have developed is that they are not created equal. Each methodology has certain limitations that must be considered by the appraiser when determining what methodologies are suitable for the particular property and when evaluating the weight to give the results of that methodology. Choosing the most accurate methodology for a particular property is a matter of professional judgment—a judgment that must be exercised for each particular property, because different characteristics and

available data may warrant rejection of a specific methodology. *Supra*, at 9-12. Where professionals reach different judgments about the best methodology for a particular property, the decision about which methodology best approximates true market value is a quintessential factual question that ought to be determined by the district court.

In the Eleventh Circuit's view, however, railroads would be forbidden from challenging even the most inapposite methodologies. For example, while some appraisers suggest that a market value for a railroad may be derived by measuring the market price of its stocks and bonds, see *supra*, at 9-10, this approach is "generally dubious and unreliable evidence" of market value, in part because "[t]here is no reliable relationship between the constantly fluctuating market of stocks and bonds and the tangible and intangible assets reflected by such securities." Ring & Boykin, *supra*, at 426; JA 122. Appraisers generally use this method to check the reasonableness of other estimates, not as an independent basis for valuing property. Ring & Boykin, *supra*, at 426. If the Eleventh Circuit's rule were to prevail, the railroad would be powerless to prove in court that a stock-and-debt method cannot reliably estimate "true market value."

Similarly, the cost approach "is poor evidence of system value for railroads," largely because of the difficulty of accurately measuring the effects of property depreciation and obsolescence. S. Rep. No. 87-445 at 456; Ring & Boykin, *supra*, at 422 ("Cost . . . no longer provides an accurate measure of value" for railroads); JA 67-68. But under the Eleventh Circuit's rule, a State could place exclusive or principal reliance on a cost approach with impunity. See *Consol. Rail Corp.* v. *Town of Hyde Park*, 47 F.3d 473, 475, 480 (2d Cir. 1995) (noting in a subsection (b)(1) case New York's reliance on "the 'cost approach' method for determining true market value" in 1993). Railroads would be unable to present their own, better evidence of value and would instead be restricted to quibbling about the calculations made in methodologies

that might have fundamental theoretical flaws when applied to railroads. Without warrant in the text of the statute, the Eleventh Circuit's rule converts the district court into a glorified fact- and math-checker, unable to correct the blatant discrimination flowing from the inherent distortions of the State's chosen methodology. As the Fourth Circuit recognized:

> It would be incongruous to accord railroads access to the full range of the court's equitable powers and then to deprive them of the principal means to benefit from that access. If denied the ability to present evidence on the true market value of its property, a railroad's rights under § 306 would be, as [the plaintiff-railroad] aptly summarized, "limited to checking the state's arithmetic."

Richmond, Fredericksburg & Potomac R.R. v. *Forst*, 4 F.3d 244, 250 (4th Cir. 1993).

The Eleventh Circuit's concept of a "true market value" calculated without regard to the inaccuracy and distortion of the valuation method employed is an oxymoron. In *Oklahoma Tax*, this Court rejected proposed constructions of "'true market value'" as "'state determined market value'" (or state determined market value absent intentional discrimination) because they were irreconcilable with the plain language of section 11501. 481 U.S. at 461-63. The Eleventh Circuit's variant – that "true market value" means "state-determined market value, with factual errors in the subsidiary calculations corrected" – is equally indefensible. The Eleventh Circuit's rule impermissibly "depends upon the addition of words to a statutory provision which is complete as it stands." *Id.* at 463.

C. Other Provisions Of The Statute Confirm The Plain Meaning Of Section 11501(b)(1).

Statutory provisions are interpreted in light of their surrounding provisions, *Dolan* v. *U.S. Postal Serv.*, 126 S. Ct. 1252, 1257 (2006); 2A Norman J. Singer, *Sutherland Statutes and Statutory Construction* § 47:6 (6th ed. 2006), and the sur-

rounding provisions in the 4-R Act confirm the plain meaning of § 11501(b)(1). First, subsection (c) states that "[t]he burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. § 11501(c). "It would be inconsistent to allocate the burden of proof as to an issue which could not be litigated in federal court in the first place." *Okla. Tax*, 481 U.S. at 462. As noted above, Congress did not require proof of "true market value" as an element of a discrimination claim, but then preclude the railroad from offering fundamental evidence of true market value.

Second, subsection (c)'s provisions regarding proof of the market values of other commercial and industrial property underscore that the district court is to determine the true market value of property independently, regardless of what methods the state appraiser employs. Because there are a multitude of commercial and industrial properties in a State, Congress authorized a specific statistical sampling method for the district court to use in determining the assessed-value/market-value ratio of such properties. Subsection (c) provides that this ratio is to be proved "*to the satisfaction of the district court*" by a "random-sampling method known as a sales assessment ratio study," and provides alternative benchmarks of discrimination if that cannot be done. 49 U.S.C. § 11501(c) (emphasis added). As this Court stated in *Oklahoma Tax*, subsection (c) constitutes an explicit "grant of authority to district courts to use statistical methods for establishing the assessed and market values of 'other commercial and industrial property' where such methods will result in proof '*to the satisfaction of the district court.*'" 481 U.S. at 462 (quoting 49 U.S.C. § 11501(c)) (emphasis added). Congress thus provided that the district court is to make its own findings of the assessed-to-market value ratio of other commercial and industrial property without regard to the valuation methods the State employed in assessing those properties. By necessary implication, the "true market value of railroad transportation property" is likewise to be determined "to the satisfaction of

the district court," without slavish deference to the state appraiser's methodological choices. See *id.* at 462-63 (Congress's specification of "particular means" for proving the value of commercial and industrial property "raises no implication whatever that the value of another kind of property may not be proved at all").

States have no more "policy" stake in valuing railroad transportation property than other commercial and industrial property for tax assessments. Subsection (c) confirms that courts are not concerned with "the methods" the State uses to value property in adjudicating a federal discrimination claim under the 4-R Act. In subsection (b)(1), the "true market values" of both railroad transportation property and other commercial and industrial properties are to be independently determined by the district court as questions of fact, and the district court's role is not one of merely correcting factual errors in the state appraiser's valuation.

D. The Eleventh Circuit's Exclusionary Rule Defeats The 4-R Act's Purpose Of Preventing Tax Discrimination.

"Statutory construction . . . is a holistic endeavor," *United Sav. Ass'n* v. *Timbers of Inwood Forest Assocs.*, 484 U.S. 365, 371 (1988), and thus this Court will look not only to the ordinary meaning of specific terms but also "'to the provisions of the whole law, and to its object and policy.'" *Massachusetts* v. *Morash*, 490 U.S. 107, 115 (1989) (quoting *Pilot Life Ins. Co.* v. *Dedeaux*, 481 U.S. 41, 51 (1987)).

The Eleventh Circuit's rule ignores the context in which the 4-R Act was enacted. See *Pfizer, Inc.* v. *Gov't of India*, 434 U.S. 308, 313 (1978) ("the context" "of the statute" is an "aid[] to construction"). Section 11501(b)(1) is a sweeping antidiscrimination statute, prohibiting discrimination-in-fact (whether intentional or not) in tax assessments and valuations against railroads. *Okla. Tax*, 481 U.S. at 462-63. The 4-R Act was designed "'to put an end to the widespread practice

of treating for tax purposes the property of [railroads] on a different basis than other property in the same taxing district,'" S. Rep. No. 91-630, at 2, 6 (noting "ominous trend" toward new and "effective means of perpetuating tax discrimination").

Congress did not enact a self-defeating antidiscrimination statute. The seminal 1961 Doyle Report stated that state tax discrimination against railroads "results" in large measure from "outmoded assessing procedures" employed at the state level. S. Rep. No. 87-445, at 448. The Report noted that "'the applicable [state] statutes contain few guideposts for the assessor or prescription of the factors, and the weight to be accorded thereto, in arriving at 'full value' of railroad—or any other—real estate,'" and railroad property is "'often valued under divergent theses, processes and procedures and too often inconsistently from year to year.'" *Id.* at 568.

Moreover, "[d]ifferent methods are employed by the various States to find value," many of which were inferior to more appropriate techniques such as a capitalization-of-earnings valuation. *Id.* at 455, 476. Indeed, Congress was aware that States often chose these inferior valuation approaches for the sole purpose of inflating the tax obligations of railroads:

> Despite the inferior quality of cost as evidence of value one of the reasons it remains in use is that cost is usually a higher figure for railroads than current cash value and the temptation to use cost figures on railroads is sometimes influenced by a desire to justify a higher full value which will in turn appear to produce a lower equalized assessment ratio.

Id. at 456-57, 479. Contrary to the Eleventh Circuit's conception, Congress did not insulate from judicial scrutiny the very practices—the choice and weighting of various appraisal methodologies and techniques—that were a root cause of the discrimination that Congress sought to redress. Rather, as

this Court has declared, subsection (b)(1) "set[s] forth *precise standards for judicial scrutiny of challenged rate and assessment practices*." *ACF*, 510 U.S. at 343 (emphasis added).

The Georgia experience is illustrative of the gaping enforcement loophole that the Eleventh Circuit's rule opens. In 2002, as noted above, the appraiser changed his valuation approach, increasing the estimate of CSXT's unit value to $8.2 billion and its Georgia taxable value of CSXT's railroad transportation property to $514.9 million (increases of 47% and 36% respectively over the 2001 values). *Supra*, at 14-15. In 2006, a new in-house employee in Georgia changed the appraisal method, and declared CSXT's unit value as $11.2 billion and its Georgia taxable value as $762 million.[12] The latter was a 40.6% increase over the 2005 Georgia taxable value. Georgia's 2006 change in the method of appraising railroad property did not affect CSXT alone. It resulted in an average Georgia taxable value increase of 46.6% for properties of all railroads operating in the State. See State Bd. of Equalization, *Public Utility and Airline Flight Equipment Digest* 2 (2006). By contrast, the average Georgia taxable value for all other centrally assessed properties increased by only 5.6%. See *id.* Congress did not handcuff district courts in remedying such discrimination, based on the artificial distinc-

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[12] Similarly, in 2006 (after the record in this case was closed), the Kentucky tax authority, using solely the disfavored stock-and-debt method, initially presented CSXT with a unit valuation of about $13.5 billion. Kentucky later agreed to reduce the unit valuation.

Florida also dramatically increased CSXT's unit value in 2006 to $14.8 billion. Complaint Seeking Injunctive and Declaratory Relief from Ad Valorem Tax Discrimination (2006 Taxes) ¶ 16, *CSX Transp., Inc.* v. *Dep't of Revenue*, No. 4:06-CV-342SPM (N.D. Fla. filed July 18, 2006). Unlike Kentucky, Florida refused to settle for a lower number with CSXT, and when CSXT brought suit under subsection (b)(1), Florida's answer relied upon the district court decision below in affirmatively alleging that CSXT could not challenge the State's chosen valuation methodology. Answer to the Plaintiff's Complaint ¶¶ 34, 41, *CSX Transp., Inc.* v. *Dep't of Revenue*, No. 4:06-CV-342SPM (N.D. Fla. filed Aug. 8, 2006).

tion drawn by the Eleventh Circuit between "factual determinations" and "nonfactual determinations" in valuation.

Moreover, the Eleventh Circuit's exclusionary rule is logically inconsistent with the longstanding rule under the 4-R Act that district courts shall make independent inquiry into the true market value of other commercial and industrial property for the tax year in question, regardless of the State's valuation procedures. Some of the most egregious discrimination before and after the 4-R Act was passed arose from state laws and practices requiring railroad property to be revalued more frequently than other commercial and industrial property. As one witness testified to Congress, "[t]he railroads are assessed every year and so their value keeps pace. Local property, real estate and so on, is typically assessed only at periodic intervals, most frequently on a quadrennial basis, although in Indiana, for example, every 8 years." *State Tax Discrimination Against Interstate Carrier Property, Hearing Before the Subcomm. on Surface Transp. of the Sen. Comm. on Commerce on S. 2289*, 91st Cong. 63 (1969) (statement of Rolf A. Weil, President, Roosevelt University); *id.* at 67; *Common and Contract Carrier State Property Tax Discrimination, Hearing Before the Subcomm. on Transp. & Aeronautics of the H. Comm. on Interstate & Foreign Commerce*, 91st Cong. 87 (1970) (statement of Rolf A. Weil, President, Roosevelt University) (same); *Louisville & Nashville R.R.* v. *Pub. Serv. Comm'n*, 493 F. Supp. 162, 163-68 (D. Tenn. 1978) (detailing abuses prior to the 4-R Act), *aff'd*, 631 F.2d 426 (6th Cir. 1980). Such regimes have the discriminatory effect that "the interstate carriers pay higher taxes than most other commercial and industrial taxpayers because their assessments reflect current increases in true market value while delayed assessment of other property delays increases in their tax assessments." Scott M. Schoenwald, Note, *Discriminatory Demands and Divided Decisions: State and Local Taxation of Rail, Motor, and Air Carrier Property*, 39 Vand. L. Rev. 1107, 1119-20 (1986).

Courts properly construed the 4-R Act to require an independent judicial determination of the fair market value of other commercial and industrial property for the tax year in question, notwithstanding state statutes that set the present market value of such property based on prior-year valuations. See *Clinchfield R.R.* v. *Lynch*, 700 F.2d 126, 130 (4th Cir. 1983) (finding a 4-R Act violation because by statute in North Carolina "the real properties of other commercial and industrial taxpayers were assessed at 72 percent of actual value, while the railroads were taxed at essentially full value"); *Atchison, Topeka & Santa Fe Ry.* v. *Lennen*, 732 F.2d 1495, 1499 (10th Cir. 1984).

Claims of contrary "state valuation policy" (even when such policy is embodied in statutes) did not and cannot preclude independent judicial determination of the assessed-to-true market value ratio of commercial and industrial property in a given tax year. The same principle applies on the other side of the equation in determining the assessed-to-fair market value of rail transportation property.

Under the proper interpretation of the 4-R Act, federal courts can remedy discrimination by finding the "true market value" of each kind of property in a given year, and determining whether the ratios of assessed-to-market value of the two kinds of property diverge by more than 5 percent. The decision below, which forbids that independent judicial inquiry, cannot be reconciled with the text or object of the Act.

E. The Eleventh Circuit's Rule Is Unworkable.

Finally, the Eleventh Circuit's rule must be rejected because it is unworkable. The rule allows a railroad to contest any factual determination the state appraiser made in employing a particular valuation technique, but not any "nonfactual determinations." JA 260. Such protected nonfactual determinations include not only the state appraiser's choice of estimation techniques, but also his weighting of the results yielded by the different techniques. JA 261.

The problem is that, if the district court cannot depart from the weighting the State would give to various estimates, simply correcting factual errors of the appraiser in applying a particular technique does not allow the district court to make a finding of "true market value" of railroad property. For example, assume a state appraiser had calculated estimates of railroad unit value as $8 billion, $10 billion, and $12 billion under income, sales, and costs approaches, and had set the value as $9.5 billion. If the district court then finds factual error in the state appraiser's estimate under the income approach, and finds that the estimate under that approach should have been $5 billion rather than $8 billion, the district court is powerless to make a finding of "true market value" that accounts for that correction. Under the Eleventh Circuit's rule, the court cannot engage in its own weighting of estimated values, and no weighting rule can generally be extrapolated from the state's prior valuation and applied to the judicially redetermined value estimates. See JA 191-193 (Mr. Dickerson's testimony that his ultimate valuation was a matter of judgment, and not the product of any specific weighting of the different value estimates). The Eleventh Circuit commands deference to so-called state "policy" choices, but it is impossible to identify the state policy to which the district court should defer. This simply underscores that valuation is an issue of professional judgment for a specific property, not a question of policy. The Eleventh Circuit's rule is a contrivance inconsistent with any rational administration of the 4-R Act.

The only proper interpretation of the 4-R Act is that the district court is to make an independent finding of "true market value," based on the adversarial presentation of evidence, including what techniques are properly employed to generate evidence of value; what the proper calculations are under those techniques; and how the values generated should be weighted in arriving at an ultimate estimation of the value of the property in question. Only after the determination is

made can the court undertake a meaningful assessment of whether the State discriminates in its tax assessment of the railroad property.

II. THE "CLEAR STATEMENT" CANON DOES NOT APPLY TO SECTION 11501(b)(1).

Despite the absence of any textual warrant in the statute, the Eleventh Circuit claimed that its exclusionary rule was compelled by *Gregory* v. *Ashcroft*, which requires a clear statement from Congress if it "'intends to alter the usual constitutional balance between the States and the Federal Government.'" JA 254 (quoting 501 U.S. at 461-62). The *Gregory* clear-statement canon has no application here, and cannot justify the decision below, for multiple reasons.

First, the *Gregory* canon does not apply here because section 11501(b)(1) is unambiguous. *Gregory*, 501 U.S. at 464-65 (clear statement canon applies only when statute is ambiguous); *Salinas* v. *United States*, 522 U.S. 52, 59-60 (1997); *United States* v. *Lopez*, 514 U.S. 549, 610-11 (1995); *McElroy* v. *United States*, 455 U.S. 642, 657 (1982). The *Gregory* canon resolves congressional intent when a statutory term is "susceptible of two plausible interpretations, one of which would have altered the existing balance of federal and state powers." *Salinas*, 522 U.S. at 59. The Eleventh Circuit did not suggest that (absent federalism concerns) the term "true market value" can be plausibly interpreted to mean the state appraiser's valuation of the property, adjusted for factual error in any of the underlying estimation techniques he used. See *id.* at 60 ("A statute can be unambiguous without addressing every interpretive theory offered by a party."). The Eleventh Circuit's exclusionary rule is simply a limitation on the railroad's proof to vindicate perceived state interests, which the court felt free to write into the statute because (in its view) "[t]he text of the Act does not clearly state that railroads may challenge valuation methodologies." JA 257. But the *Gregory* canon "'is not a license for the judiciary to rewrite lan-

guage enacted by the legislature.'" *Salinas*, 522 U.S. at 59-60.[13]

Second, this Court in *Oklahoma Tax* rejected the invocation of "comity" with the States in holding that the meaning of "'true market value'" in section 11501(b)(1) was plain and could not be construed to mean "'state determined market value'" or "state determined market value" absent intentional discrimination (the alternatives proposed by respondents and the court of appeals in that case). *Okla. Tax*, 481 U.S. at 461-64. Once Congress has weighed the "policy considerations," courts are "not free to reconsider them now." *Id.* at 464.

Third, Congress has already balanced federal and state interests in § 11501(b)(1). As this Court has recognized, "the whole of § 1150[1] sets limits upon the taxation authority of state government." *ACF*, 510 U.S. at 345. However, these limits were carefully crafted to balance federal and state interests.

To protect the legitimate interests of the States while accomplishing its remedial goals of protecting interstate railroads against discrimination, Congress placed four specific restrictions on the exercise of this new federal jurisdiction. First, "[r]elief may be granted under this subsection only if the ratio of the assessed value to true market value of rail transportation property exceeds by at least 5 percent the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction." 49 U.S.C. § 11501(c). This 5% tolerance factor is a reasonable margin of error, and it protects taxing jurisdictions from injunctions where uncertainties in the assessment process produce undramatic variations in assessment ratios. See S. Rep. 91-630, at 14-15. Second, and relatedly, by prohibiting only that portion of a tax assessment determined to be excessive

[13] The Court did not hold in *Oklahoma Tax* that section 11501(b)(1) was ambiguous as to whether railroads could challenge accounting methods used by the state; it simply observed that the question was not raised, and so it expressed no view on the issue. 481 U.S. at 463 n.5.

under the assessment-ratio test, the statute limits federal court interference with the state-tax collection process. Pub. L. No. 94-210, § 306(1)(a), 90 Stat. 31, 54 (1976) ("but only to the extent of any portion based on excessive values as hereinafter described").[14] Third, "[t]he burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. § 11501(c). Finally, in order to give the States an opportunity to bring their taxation practices into compliance, Congress granted a grace period of three years before § 11501 went into effect. Pub. L. No. 94-210, § 306(2)(b), 90 Stat. at 54 ("the provisions of this section shall not become effective until 3 years after the date of enactment of this section").

"Congress has exercised its Commerce Clause authority to regulate rail transportation for over a century." *Pittsburgh & Lake Erie R.R.* v. *Ry. Labor Executives' Ass'n*, 491 U.S. 490, 510 (1989). The balance to be struck between protection of interstate commerce and sensitive state interests is largely committed to the political process itself, and in particular to the national legislature. See *Garcia* v. *San Antonio Transit Dist.*, 469 U.S. 528, 550-52 (1984). The Eleventh Circuit's judicial rewrite of section 11501(b)(1), "'while purporting to be an exercise in judicial restraint, would trench upon the legislative powers vested in Congress by Art. I, § 1, of the Constitution.'" *Salinas*, 522 U.S. at 60. A court may not second-guess Congress on the critical policy choices it made in enacting § 11501.

Fourth, the *Gregory* canon does not apply every time a federal law touches upon an aspect of state sovereign power; it applies when one among two or more permissible constructions would "'alter the "usual constitutional balance between the States and the Federal Government."'" *Gregory*, 501 U.S. at 460-61.

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[14] In codifying the original Section 306, some changes to the language were made. However, Congress did not intend a substantive change. *Okla. Tax*, 481 U.S. at 457 n.1.

Allowing a district court adjudicating a federal discrimination claim to take evidence on true market value based on different estimation techniques does not affect, much less alter, the federal-state constitutional balance. The Eleventh Circuit's characterization of Mr. Dickerson's selection and weighting of three valuation techniques for valuing CSXT's property as "delicate matters of state policy," JA 260, is strained. Mr. Dickerson was not engaged in policy choices; he was performing his ordinary duties as an appraiser, applying standard techniques to generate different "evidence of value," *NATA Report* 8, to assist him in rendering a judgment on the value of CSXT's rail transportation property. There is no special sovereign interest in one state employee's particular choice or weighting of valuation techniques for a given property. Indeed, States (including Georgia) generally leave calculation of valuation and the attendant choice of such techniques to state assessors, as opposed to legislating it, precisely because the appropriateness and weight given to any technique depends on the data available and the nature of the property.[15]

The frequent changes in the techniques the state appraiser uses belies any suggestion that the methodology is a considered state policy choice entitled to deference. For tax year 2002, Mr. Dickerson changed the valuation methods used by his predecessor by replacing the capitalized earnings approach with a discounted cash flow model, and by replacing the direct capitalization approach with a market multiple approach. JA 204-205. Later, after CSXT brought suit, Mr. Dickerson decided to prepare "a complete appraisal of CSXT using essentially the same three valuation methods that he [had] employed" earlier. JA 203. However, as the litigation progressed, he then chose to prepare "a revised full appraisal

[15] N.Y. State Office of Real Prop. Servs., *supra*. That has long been true. The Doyle Report noted that "[v]aluation or appraisal is the process by which an *assessor arrives at his opinion* of the value of the property," and that legislatures tended not to define the methods tax appraisers must use. S. Rep. No. 87-445, at 452, 458 (emphasis added).

of CSXT" in which he changed "the calculation of the cost of equity used in deriving the weighted cost of capital." *Id.* As a result of this change, Mr. Dickerson "ultimately opined that the fair market unit value of CSXT was $11.807 billion." JA 204. Moreover, in 2004, the Department, wishing to avoid litigation by major centrally-assessed taxpayers aggrieved by the excessive valuations caused by Mr. Dickerson's new methodology, chose not to use Mr. Dickerson's methods at all. See JA 152-159.

The Eleventh Circuit's invocation of the constitutional-avoidance canon of *Gregory* on the limited question of what evidence of market value a district court may consider is especially perverse given that section 11501(b)(1) itself alters the federal-state constitutional balance. At the time the 4-R Act became law, certain states had either statutory or constitutional provisions that provided for the taxation of railroad property on a higher assessed basis of market value than other commercial and industrial property. Because section 11501(b)(1) unequivocally outlawed that form of discrimination, courts declared those state tax classification schemes in violation of the 4-R Act and granted relief to the railroads. *Arizona* v. *Atchison, Topeka & Santa Fe Ry.*, 656 F.2d 398 (9th Cir. 1981); cf. *Louisville & Nashville R.R.* v. *Pub. Serv. Comm'n*, 493 F. Supp. 162 (M.D. Tenn. 1978) (relief granted under Equal Protection Clause, since 4-R Act not yet in effect), *aff'd*, 631 F.2d 426 (6th Cir. 1980). Congress thus altered the constitutional balance when it prohibited forms of discrimination sanctioned by state statutes and even state constitutions. Given Congress's decision to enact such an anti-discrimination statute, there is no substantial constitutional question to avoid by preventing district courts from determining "true market value" of railroad property based on different valuation techniques than those chosen by a state appraiser.

Fifth, Department of Revenue of Oregon v. *ACF Industries, Inc.*, 510 U.S. 332 (1994), relied on by the Eleventh Circuit,

JA 257, is not to the contrary. At issue in *ACF* was subsection (b)(4), which prohibits "another tax that discriminates against a rail carrier." 49 U.S.C. § 11501(b)(4). The question presented was whether that broadly worded provision outlawed the longstanding practice of creating state tax exemptions from *ad valorem* property taxes for certain other classes of commercial and industrial property. 510 U.S. at 339-40.

Although the Court noted that "[b]oth the State's and the [taxpayers'] readings are defensible if subsection (b)(4) is read in isolation," the Court found that "[t]he structure of § [11501] as a whole does yield an answer, one adverse to the [taxpayers'] challenge to Oregon's property tax." *Id.* at 339-40. The Court held that the taxpayers' reading of subsection (b)(4) would nullify (b)(3), and that the statutory definition of "'commercial and industrial property'" encompassed only "taxed" (*i.e.*, nonexempt) property. *Id.* at 340-43. Indeed, the Court did not invoke *Gregory* at all (because there was no question that section (b)(4) did, by prohibiting all tax discrimination not otherwise addressed in (b)(1)-(3), alter the federal-state balance). Rather, the Court invoked the related federalism-based canon against interpreting a federal statute preempting traditional state powers beyond its "evident scope." *Id.* at 345 (citing, inter alia, *Rice* v. *Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)).

Critically, in contrast to the absence in (b)(4) of express textual support for the taxpayers' position or standards for adjudicating discrimination claims, *id.* at 343, the *ACF* Court observed that

> *[t]he reach of subsections of (b)(1)-(3) is straightforward:* These provisions forbid the imposition of higher assessment ratios or tax rates upon rail transportation property than upon "other commercial and industrial property."

Id. at 337 (emphasis added). In subsections (b)(1)-(3), "Congress prohibited discriminatory tax rates and assessment ra-

tios *in no uncertain terms*, and set forth *precise standards for judicial scrutiny of challenged rate and assessment practices*." *Id.* at 343 (internal citations omitted) (emphasis added). As explained in *Oklahoma Tax*, one of those "precise standards for judicial scrutiny" is the subsection (b)(1) formula, which requires a determination of the railroad property's "true market value." See 481 U.S. at 461-62. Thus, unlike *ACF*, this case involves no attempt "to extend the statute beyond its evident scope." 510 U.S. at 345. It is the evident plain meaning and purpose of (b)(1) that the Eleventh Circuit's exclusionary rule subverts.

Finally, there is no federalism concern remotely comparable to that raised in *ACF*, where a State's power to exercise the critical legislative power of granting tax exemptions was in jeopardy. Here, the only question is whether the district court may make an independent determination of "true market value" of CSXT's rail transportation property by considering evidence generated by different valuation techniques from those the state appraiser employed.

III. THE LEGISLATIVE HISTORY OF THE 4-R ACT SUPPORTS THE PLAIN LANGUAGE.

When Congress has spoken plainly to the matter at hand, as it has done with § 11501(b)(1), the Court's inquiry comes to an end and resort to legislative history is unnecessary. *Okla. Tax*, 481 U.S. at 461. Even though this Court found the legislative history "inconclusive and irrelevant" to the interpretation of section 11501(b)(1), *id.*, the court below purported to find support for its exclusionary rule in that history. JA 257. The Eleventh Circuit was mistaken, and indeed that history shows only that adoption of its position would amount to a judicial award of victory to opponents of the Act who lost legislatively three decades ago.

1. Throughout the debate on proposed legislation, it was well understood that allowing railroads to attack discriminatory taxes by proof of "true market value" would entail judi-

cial scrutiny of state valuation procedures. For example, dissenting Senator Lausche of Ohio attached a statement to a Senate report objecting to the breadth of a precursor bill, S. 927, because "[u]nder S. 927, a Federal court will necessarily be required to *review State valuation principles and procedures* in order to determine whether carrier operating property is assessed at a percentage of true market value that is higher than the assessment percentage of all other property." S. Rep. No. 90-1483, at 26 (emphasis added).

Similarly, George Kinnear, Director of the Washington State Department of Revenue, noted that "it would be immediately necessary under this bill for Federal courts to *review and determine the correctness of . . . valuation procedures* and the actual valuation results for the carriers." *State Tax Discrimination Against Interstate Carrier Property: Hearing Before the Subcomm. on Surface Transp. of the S. Comm. on Commerce on S. 2289*, 91st Cong. 99 (1969) (letter from George Kinnear, Director, Washington State Dept. of Revenue) (emphasis added) (emphasis in original omitted); see also *id.* ("I am deeply concerned that this very broad statutory language is an open invitation, and perhaps even a requirement, for a *Federal judge to determine de novo the true market value of transportation property*") (emphasis added). Indeed, Mr. Kinnear's proposed amendment to define "true market value" as "that true market value finally determined in accordance with state statutory procedures," *id.* at 101-02, was never adopted. See 116 Cong. Rec. 2022, 2024 (1970). The Eleventh Circuit has by judicial revision written Mr. Kinnear's proposed amendment back into the statute.

Finally, there is no suggestion that Congress diluted the impact of the proposed legislation at any time between the reports and hearings of the 1960s and the ultimate enactment of Section 11501(b)(1) in 1976. To the contrary, the changes that were made to the legislation only reaffirm the plain meaning of Section 11501(b)(1). For example, the provision prescribing a burden of proof for determining true market

value, 49 U.S.C. § 11501(c), was added in the 1970s, reaffirming Congress's recognition that true market value would be a factual issue in § 11501 cases and that federal courts would determine true market value as they would in any other valuation case. See S. Conf. Rep. No. 94-595, at 27, 166 (1976); S. Rep. 94-499, at 65, 150; S. Conf. Rep. 94-585, at 24, 139 (1975); S. Rep. 92-1085, at 3, 7.

2. Against this exhaustive legislative history, the court below pointed to two isolated snippets from early in the Act's legislative history as support for its reading that Congress did not intend courts independently to assess methodologies as part of determining true market value. See S. Rep. No. 90-1483, app. B at 22 (1968); *Common and Contract Carrier State Property Tax Discrimination: Hearing on H.R. 16245 Before the Subcomm. on Transp. and Aeronautics of the H. Comm. on Interstate and Foreign Commerce*, 91st Cong. 132-33, 137-38 (1970) (statement of Philip M. Lanier, Association of American Railroads).

The court below misread these snippets. The testimony simply explained that the proposed legislation

> does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves. It merely provides a single standard against which all affected assessments must be measured in order to determine their relationship to each other. It is not a standard for determining value; it is a standard to which values that have already been determined must be compared. This standard is "true market value" (also the generally accepted standard for assessment purposes) and the requirement is that carrier property be assessed at the same proportion of such value as the proportion at which all other property subject to the same tax rates is assessed.

S. Rep. 90-1483, app. B at 22. Thus, "true market value" was not an assessment method or practice that the States were be-

ing required by Congress to adopt. States could continue to use whatever methods they liked; courts could not issue injunctions dictating what valuation and assessment methods States must use going forward in imposing taxes.

Instead, whatever methods the State employs, the end result is measured against 49 U.S.C. § 11501(b)(1), which prohibits discrimination against interstate railroads and provides that "true market value" is the standard to which State assessments must be compared. The Lanier testimony is plain: "values that have already been determined must be compared to" the federal standard of "true market value" found by the district court. Thus, railroads are entitled to introduce valuation evidence—including evidence based on valuation methods that are different from the methods used by state appraisers—in order to prove the existence and degree of discrimination. And consistent with the statute's proscriptions, the court may only enjoin a State in violation of the 4-R Act from collecting the excess revenue. The 4-R Act is thus quite deferential to States; it prohibits discrimination, but does not otherwise dictate how the State exercises its power to tax property within the State.

In summary, the Eleventh Circuit's exclusionary rule is irreconcilable with the language, structure, purpose, and history of section 11501(b)(1); is not compelled by federalism principles; and simply operates to vitiate the federal discrimination remedy that Congress created to protect interstate railroads. This Court should reject it.

CONCLUSION

For the foregoing reasons, the judgment should be reversed and the case remanded for a new trial.

Respectfully submitted,

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
MATTHEW J. WARREN
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Ave., NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON,
BEARMAN, CALDWELL
& BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

* Counsel of Record

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In The

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA; BART L. GRAHAM, AS COMMISSIONER OF REVENUE OF THE STATE OF GEORGIA; RUSSELL W. HINTON, AS STATE AUDITOR OF THE STATE OF GEORGIA; AND GENA L. ABRAHAM, AS DIRECTOR OF THE GEORGIA STATE PROPERTIES COMMISSION,

Respondents.

On Writ Of Certiorari To The
United States Court Of Appeals
For The Eleventh Circuit

BRIEF OF RESPONDENTS

THURBERT E. BAKER
Attorney General

WARREN R. CALVERT
Senior Assistant
Attorney General
(*Counsel of Record for Respondents*)

R. O. LIKER
Deputy Attorney General

Attorneys for Respondents

GEORGIA DEPARTMENT OF LAW
40 Capitol Square, S.W.
Atlanta, Georgia 30334-1300
(404) 656-3347

PETER J. CROSSETT
JOHN D. COOK
HISCOCK & BARCLAY, LLP
One Park Place
300 South State Street
Syracuse, New York
13202-2078
(315) 425-2814

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTION PRESENTED FOR REVIEW

Whether a railroad, in an action under 49 U.S.C. § 11501(b)(1) claiming that the State has overvalued its transportation property for tax purposes, is limited to disputing the way in which the State has applied a reasonable valuation methodology or may challenge the methodology itself by asking that true market value be recalculated under a different methodology.

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STATEMENT OF THE CASE

I. Nature Of The Litigation And Question Presented

Petitioner CSX Transportation, Inc. ("CSXT"), an interstate common carrier by rail, filed the instant action in September 2002 against the Georgia State Board of Equalization and its individual members, including the State Revenue Commissioner,[1] challenging the State's proposed assessment of the railroad's operating property for 2002 ad valorem tax purposes under Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, 90 Stat. 54 (Feb. 5, 1976) ("the 4-R Act"), currently codified at 49 U.S.C. § 11501.[2] CSXT contended that the State's proposed assessment violated Section 11501(b)(1), which prohibits

> assess[ing] rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment

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[1] For simplicity purposes, the Respondents will hereinafter be referred to collectively as "the State."

[2] The language of the original § 306, first codified at 49 U.S.C. § 26c (1976 ed.), was slightly revised when the provision was recodified in 1978 (49 U.S.C. § 11503) and then again in 1995 (49 U.S.C. § 11501). The revisions were not intended to make a substantive change in the law. *Burlington N. R.R. Co. v. Okla. Tax Comm'n*, 481 U.S. 454, 457 n.1 (1987) (1978 revision "may not be construed as making a substantive change in the laws replaced"); H.R. Conf. Rep. No. 104-422, at 878 (1995) ("This provision [Section 11501] replaces without substantive change former section 11503.") For convenience, further citations to the statute refer to the text of its current version in 49 U.S.C. § 11501 ("Section 11501").

> jurisdiction has to the true market value of the other commercial and industrial property.

CSXT argued that the State had significantly overvalued its transportation property, resulting in a ratio of assessed value to true market value for that property of approximately 55%, while other commercial and industrial property was assessed at only 40% of its value. Jt. App. 11, 12.

In *Burlington Northern Railroad Co. v. Oklahoma Tax Comm'n*, 481 U.S. 454 (1987) ("*Oklahoma Tax*"), this Court held that Section 11501 permitted review by federal courts of alleged overvaluation of railroad properties by state tax authorities. But the Court expressly left open the legal question presented here. Oklahoma's tax officials had derived the railroad's value by taking a weighted average of original cost and capitalized net operating income. *Oklahoma Tax*, 481 U.S. at 459. Although it ruled for the railroad, the Court noted that:

> Petitioner has not challenged the valuation *methodology* employed by respondents in determining the value of petitioner's railroad; petitioner's sole challenge is to the *application of that methodology*, particularly the State's evaluation of the cost of capital and the State's refusal to make deductions for property which petitioner claims is obsolete. Tr. Of Oral Arg. 15-16. This case therefore does not present the question of whether a railroad may, in an action under [Section 11501], challenge in the district court the appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied. Accordingly we express no view on that issue.

Oklahoma Tax, 481 U.S. at 463 n.5 (emphasis added). In this case the courts below decided that question in the State's favor. Jt. App. 208-216, 252-258.

II. The "True Market Value" Of CSXT's Transportation Property In Georgia

A. *The State's Proposed Assessment.* In valuing CSXT's operating property for 2002 ad valorem tax purposes, the Georgia Department of Revenue used the unit rule, under which it first determined the value of CSXT's railroad as an entire operating system irrespective of where the operating property was located and without functional or geographic division of the whole into its component parts. Jt. App. 26, 200. The State's proposed assessment was based on an $8.2 billion unit value estimate for CSXT, with certain deductions, which was allocated to the State using the percentage of Georgia road miles to system road miles to arrive at the Georgia taxable fair market value of the rail assets. Jt. App. 202, 248. CSXT contends, however, that the railroad's system wide unit value was only $6 billion. Jt. App. 30, 195, 250.

Mr. Gregg Dickerson, the Revenue Department's Public Utility Manager, prepared the State's proposed assessment. Mr. Dickerson had worked at the Department of Revenue for approximately 10 years preparing public utility valuations before leaving in 1993 to take a position in the tax department at Norfolk Southern Railroad.[3]

[3] Mr. Dickerson is an appraiser with over thirty years' experience, including well over one thousand valuations performed under the unit rule. Jt. App. 172-174, 246-247. He has been a frequent speaker on such topics as the income approach and the use of market multiples and stock-and-debt methods as they apply to the unit rule valuation of

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Jt. App. 175-177, 246-247. When Mr. Dickerson returned to government service in 2001 the State was calculating unit values using a yield capitalization method that divided a first year's estimated free cash flow by a cost of capital minus a growth rate; a direct capitalization method; and a stock-and-debt method. Jt. App. 177-178, 247. For the tax year 2002, the State replaced the first two methodologies with discounted cash flow ("DCF") and market multiples methods, but it kept the stock-and-debt method. *Id.*

The State also instituted a change in 2002 for railroads that was not needed for other public utilities: it began to use income figures taken from the companies' annual reports to shareholders instead of their regulatory reports to the Surface Transportation Board ("R-1 reports") to project future cash flows in its DCF analysis. Jt. App. 178-183. CSX Corporation's Vice President and Controller acknowledged at trial that management's view of the railroad's financial performance was reflected in the annual report figures and not the R-1's. Jt. App. 186-188, 190, 233. The figures in these two reports can vary greatly,[4] and the largest part of the 47% increase in CSXT's 2002 assessment over 2001 was due to that change in the income amounts used to value the company. Jt. App. 179, 233.

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public utilities, including railroads; has taught unit rule valuation methodologies at both state and national educational programs; and has been published in various national journals and digests in the property appraisal and property assessment fields. Jt. App. 142-46.

[4] For example, CSX Corporation's annual report for 2001 showed that its rail segment had operating income of $743 million, but CSXT's R-1 report to the Surface Transportation Board reflected net revenue from rail operations of only $458 million for the same period. Jt. App. 179-182.

The State's DCF analysis yielded a 2002 unit value of $8.1 billion. Jt. App. 247. Its stock-and-debt method showed a unit value of $12 billion. *Id.* Mr. Dickerson derived three indicators of CSXT's unit value using the market multiples method from the amounts that his DCF showed as the railroad's operating revenues, operating EBITDA, and operating EBIT for the tax year 2002; those unit values were $12.3 billion, $10.7 billion, and $8.4 billion, respectively. Jt. App. 248. Mr. Dickerson concluded that a unit value of $8.2 billion was at the lower end of the range within which CSXT's true value would lie, and he chose that value to avoid litigation. Jt. App. 202, 248.

B. *CSXT's Appraisal.* CSXT relied on an appraisal by Mr. Thomas Tegarden, who derived unit value estimates of $9.637 billion, $5.983 billion, and $6.15 billion using a stock-and-debt method, a yield capitalization method, and a cost method, respectively. Jt. App. 250. He gave no weight to the stock-and-debt method and little weight to his cost method in concluding that CSXT's unit value was only $6 billion. *Id.*

III. The Rulings By The Courts Below

A. *The District Court.* The district court held that it could not consider Mr. Tegarden's valuation because it was prepared under different methods than the State's.[5] Jt. App.

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[5] Nevertheless, the court expressed serious reservations about the unit value estimate of CSXT's appraiser, as it failed at least one straightforward test of reasonableness. "If, as CSXT claims, the value of CSXT was $6 billion, CSXT would have a negative equity value. CSX Corporation [the railroad's parent], however, held investment grade bond ratings implying a profitability level in excess of that needed to

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214-216. In so holding, the district court agreed with the Fourth Circuit's analysis in *Chesapeake Western Railway. v. Forst*, 938 F.2d 528 (4th Cir. 1991), *cert. denied*, 503 U.S. 966 (1992) ("*Chesapeake Western*"), and that of courts in the Eighth and Tenth Circuits, *see Union Pacific R.R. Co. v. State Tax Comm'n*, 716 F. Supp. 543 (D. Utah) ("*Union Pacific*"); *Burlington N. R.R. Co. v. Bair*, 815 F. Supp. 1223 (S.D. Iowa 1993), *aff'd*, 60 F.3d 410 (8th Cir. 1995), *cert. denied*, 516 U.S. 113 (1996) ("*Bair*"). Jt. App. 208-214. The district court recognized, of course, that it still had to "weigh the evidence and make its own factual findings regarding the true market value of CSXT." Jt. App. 214. That process was described by the court as follows:

> After parsing through days of expert testimony, the court concludes that the Department's DCF value as set out in its Proposed Valuation is the most accurate indicator of CSXT's unit value.[6] As a result, the court holds that, for purposes of applying the 4-R Act to the defendants' assessments of CSXT, the true market unit value of CSXT for the tax year 2002 was $7,726,293,350.

Jt. App. 229.[7] Using the State's track-mile allocation percentage and certain deductions, the court found that

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pay both current interest expenses and the principal balance of debt." Jt. App. 223 n.12.

[6] The court had carefully analyzed and rejected each of CSXT's myriad objections to the State's application of the DCF methodology. Jt. App. 218-221.

[7] "The court arrived at this number by taking the Department's $8,126,293,350 DCF value for CSXT and subtracting $400 million to account for CSXT's intangible property." Jt. App. 229 n.23.

"[t]he true market value of CSXT's taxable rail transportation property in Georgia for the tax year 2002 . . . was $509,560,171" and that there was no violation of Section 11501(b)(1). *Id.*

B. *The Eleventh Circuit's Decision.* The Eleventh Circuit affirmed the district court in a 2-1 decision, agreeing that CSXT could not challenge the State's valuation methodology. Jt. App. 252-258. In particular, the Eleventh Circuit upheld the district court's finding "that the appraisal prepared for the Railroad by Tegarden was based on a methodology different from the methodology used by the State." Jt. App. 260. According to the Eleventh Circuit, a valuation methodology "encompass[es] all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be." *Id.*

SUMMARY OF THE ARGUMENT

In *Burlington Northern Railroad Co. v. Oklahoma Tax Comm'n*, 481 U.S. 454 (1987), this Court expressly left open the question whether a railroad, in an action under Section 11501(b)(1) claiming that a state has overvalued its transportation property for tax purposes, is limited to disputing the way in which the state has applied a reasonable valuation methodology or may challenge the methodology itself by asking that true market value be recalculated under a different method. The Eleventh Circuit answered that question correctly in favor of the State. Section 11501(b)(1) sets limits upon state taxing authority, and well-established principles of federalism

require that Section 11501(b)(1) be construed narrowly to cover only those circumstances Congress clearly contemplated and addressed, not those where Congress' policy is uncertain. As this Court stated in *Dep't of Revenue of Or. v. ACF Industries*, 510 U.S. 332, 345 (1994), Section 11501 should not be extended "beyond its evident scope."

The statute does not "plainly" allow a railroad to challenge the true market value of its assets determined under a correctly applied, reasonable valuation method chosen by the state. Indeed, there are numerous ways in which to estimate the true market value of railroad property, and Congress did not clearly require states to use any particular method, leaving them free to choose from within the range of reasonable options available to them. In addition, Congress provided that the ratio of assessed value to "true market value" of other commercial and industrial property could be proved through a sales ratio study but did not prescribe a method for calculating that ratio for rail property. That fact indicates that Congress did not mean to take away the states' right to choose appropriate methods for estimating railroads' true market value. That reading of the statute is confirmed by the legislative history, during which railroad representatives told Congress that the Act was not meant to "require a state to change its assessment standards [or] assessment practices." Moreover, this Court's decisions approving the unit rule and formulary apportionment also recognize that states are entitled to latitude in estimating the value of taxable property within their jurisdiction, which is a latitude that CSXT would deny to states sued under Section 11501(b)(1).

CSXT claims that no workable line can be drawn between states' valuation "methods" and their "application."

However, the line between the unit rule and summation methods is clear. Nor is there, for example, a plausible argument that the stock-and-debt method is just a different "application" of a DCF method. There can be closer questions, but so far the courts have in practice been able to discern the appropriate line between different "methods" on the one hand and different "applications" of the same method on the other, even though the boundary may not always be perfectly distinct or easily described in the abstract. In order to avoid any possibility whatsoever of confusion at the margins, CSXT says that railroads should always be permitted to subject a state's valuation methodology to a battle of expert witnesses over whether it is "better" than any other method a railroad might wish to use. That solution is worse than the supposed problem, and it would turn district courts into federal boards of equalization and extend Section 11501(b)(1) well beyond its "evident scope."

ARGUMENT

I. Principles of Federalism Require That Section 11501(b)(1) Be Construed Narrowly In Favor Of A State's Right To Select Methods For Valuing Property For Tax Purposes

This Court long has recognized "the important and sensitive nature of state tax systems and the need for federal-court restraint when deciding cases that affect such systems." *Fair Assessment In Real Estate Ass'n v. McNary*, 454 U.S. 100, 102 (1981). *See also id.* at 102-03 ("the autonomy and fiscal stability of the States survive best when state tax systems are not subject to scrutiny in federal courts."). The reason for such restraint is obvious,

because "[i]t is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments, and it is of the utmost importance to all of them that the modes adopted to enforce the taxes levied should be interfered with as little as possible." *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110 (1871). This proscription against federal interference in state tax matters is part of larger principles of federalism that have been described as "a proper respect for state functions, a recognition of the fact that the entire country is made up of a Union of separate state governments, and a continuance of the belief that the National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways." *Younger v. Harris*, 401 U.S. 37, 44-45 (1971).

Section 11501 was enacted against this strong background presumption that state tax administration normally should be free from federal interference. To be sure, the statute contains an express exception to the Tax Injunction Act, 28 U.S.C. § 1341 ("TIA"), which ordinarily would bar federal jurisdiction in litigation like this as long as state law afforded a "plain, speedy and efficient remedy." *See* Section 11501(c). But the TIA is not the only reflection of this federal reluctance to intrude into state tax matters. *Nat'l Private Truck Council v. Okla. Tax Comm'n*, 515 U.S. 582, 586 (1995) ("Since the passage of § 1983, Congress and this Court repeatedly have shown an aversion to federal interference with state tax administration. The passage of the Tax Injunction Act in 1937 is one manifestation of this aversion. We subsequently relied upon the Act's *spirit* to extend the prohibition from injunctions to declaratory judgments regarding the constitutionality of state taxes.") (emphasis added)

(internal citations omitted); *id.* at 590 ("Given the strong background presumption against interference with state taxation, the Tax Injunction Act may be best understood as but a partial codification of the federal reluctance to interfere with state taxation."); *Fair Assessment*, 454 U.S. at 107 ("Because we decide today that the principle of comity bars federal courts from granting damages relief in [state tax] cases, we do not decide whether [the TIA], standing alone, would require such a result.").

The Court has held, for example, that 42 U.S.C. § 1983 does not provide a statutory basis for state courts to issue injunctive or declaratory relief in tax cases where there is an adequate state remedy at law. "The Tax Injunction Act does not prohibit state courts from entertaining § 1983 suits that seek to enjoin the collection of state taxes." *Nat'l Private Truck Council*, 515 U.S. at 588. Rather, "the Tax Injunction Act reflects the congressional concern with *federal* court interference with state taxation, and there is no similar statute divesting state courts of the authority to enter an injunction under federal law when an adequate legal remedy exists." *Id.* at 590 (internal citation omitted). The Court nevertheless concluded in *National Private Truck Council* that

> [i]n determining whether Congress has authorized state courts to issue injunctive and declaratory relief in state tax cases, we must interpret § 1983 in light of the strong background principle against federal interference with state taxation. Given this principle, we hold that § 1983 does not call for either federal or state courts to award injunctive and declaratory relief in state tax cases when an adequate legal remedy exists.

Id. at 589. *Accord General Motors Corp. v. City and County of San Francisco*, 81 Cal. Rptr. 2d 544, 551 (Cal. Ct. App. 1999) ("the principle of federal constraint in the area of state taxation applies not only to federal courts but also to [the interpretation of] federal legislation," citing *Nat'l Private Truck Council*, 515 U.S. at 589). Section 11501 must be construed with that same background principle in mind, even though the TIA itself does not bar this litigation. Moreover, as an exception to the broader policy of federal non-interference only partially codified in the TIA, Section 11501 should be read to extend only to those circumstances Congress clearly contemplated and addressed, not to those where Congress' policy is uncertain. *See California v. Grace Brethren Church*, 457 U.S. 393, 413 (1982) ("In order to accommodate . . . concerns [about interfering with the operation of state tax systems] . . . we must construe narrowly the 'plain, speedy and efficient' exception to the Tax Injunction Act.").

This Court already has recognized that these rules of statutory construction apply in interpreting Section 11501. In *Department of Revenue of Oregon v. ACF Industries*, 510 U.S. 332 (1994) ("*ACF Industries*"), the Court held that Section 11501(b)(4) – which prohibits the imposition of "another tax that discriminates against a rail carrier providing transportation" – does not limit a state's discretion to exempt non-railroad property from generally applicable ad valorem property taxes.

> Principles of federalism support, in fact compel, our view. [Section 11501] sets limits upon the taxation authority of state government, an authority we have recognized as central to state sovereignty. When determining the breadth of a federal statute that impinges upon or pre-empts

> the States' traditional powers, we are hesitant to extend the statute beyond its evident scope. We will interpret a statute to pre-empt the traditional state powers only if that result is "the clear and manifest purpose of Congress." As explained above, neither [the particular subsection] nor the whole of [Section 11501] meets this standard with regard to the prohibition of property tax exemptions.

ACF Industries, 510 U.S. at 345 (internal citations omitted). Section 11501(b)(1) therefore should be construed narrowly in favor of a state's right to select for itself a reasonable method for valuing railroad property.[8] *See* Jt. App. 257 ("Based on the reasoning of the Court in *ACF Industries*, we conclude that railroads may not challenge state methodologies under subsection (b)(1).")

This same recognition of and respect for the place that the individual states occupy as sovereigns along with the United States in our federalist system of government is reflected in the "clear statement rule," upon which the Eleventh Circuit relied in its ruling below. *See* Jt. App. 257 ("The text of the Act does not clearly state that railroads may challenge valuation methodologies. Without that clear statement of congressional intent, the argument of the

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[8] The district court correctly noted that the DCF, stock-and-debt, and market multiples approaches used by the State in this case are "widely accepted and used by valuation experts." Jt. App. 212. *See also Discriminatory Taxation of Common Carriers: Hearings on S. 927 Before the Subcomm. on Surface Transportation of the S. Comm. on Commerce*, 90th Cong. 66 (1967) ("Highly refined techniques exist for measuring railroad values using such techniques as capitalizing railroad operating income, using the market values of stocks and bonds, and determining depreciated reproduction costs.") (statement of Rolf A. Weil, President, Roosevelt University).

Railroad fails.") It cannot be presumed that Congress intended to regulate the "substantial sovereign powers" of states unless the federal statute in question is unmistakably clear in that regard. As this Court has stated, "in traditionally sensitive areas, such as legislation affecting the federal balance, the requirement of clear statement assures that the legislature has in fact faced, and intended to bring into issue, the critical matters involved in the judicial decision." *Gregory v. Ashcroft*, 501 U.S. 452, 461 (1991) (citations and internal quotation marks omitted). Under the clear statement principle, "if Congress intends to alter the usual constitutional balance between the States and the Federal Government, it must make its intention to do so unmistakably clear in the language of the statute." *Id.* at 460-61 (quoting *Atascadero State Hosp. v. Scanlon*, 473 U.S. 234, 242 (1985)) (internal quotation marks omitted). Indeed, Congress' intent must be " 'clear and manifest' if it intends to pre-empt the historic powers of the States." *Will v. Mich. Dep't of State Police*, 491 U.S. 58, 65 (1989) (quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)). "This plain statement rule is nothing more than an acknowledgment that the States retain substantial sovereign powers under our constitutional scheme, powers with which Congress does not readily interfere." *Gregory*, 501 U.S. at 461. This principle has been applied in a variety of contexts involving federal regulation of the "substantial sovereign powers" of the States. *See, e.g., Raygor v. Regents of Univ. of Minn.*, 534 U.S. 533, 543-44 (2002) (whether the federal supplemental jurisdiction statute tolls the statutes of limitation for state law claims in state court); *Kimel v. Fla. Bd. of Regents*, 528 U.S. 62, 73-74 (2000) (whether a federal statute abrogates state sovereign immunity); *Gregory*, 501 U.S. at 461-67 (whether the federal Age Discrimination in Employment

Act applies to state judges); *Will*, 491 U.S. at 65 (whether states are "persons" that may be sued under 42 U.S.C. § 1983); *Rice*, 331 U.S. at 230 (whether a federal statute preempts state law).

CSXT maintains that federalism concerns are inapplicable here because "this Court in *Oklahoma Tax* rejected the invocation of 'comity' with the States." Pet. Brief, p. 42. In fact, the Court disagreed with state officials' broad claim in *Oklahoma Tax* that a railroad could never dispute the state's valuation in an action under Section 11501(b)(1), holding that principles of federalism could not support that position because the statute unambiguously allowed an overvaluation claim:

> Respondents contend that injunctive relief against state taxation offends the principles of comity. The Court of Appeals found that its restrictions on valuation actions under [§ 11501] are necessary in order to avoid "an inevitable clog of federal dockets" and "unreasonable delay of the state tax collection process." These are policy considerations which may have weighed heavily with legislators who considered the Act and its predecessors. It should go without saying that we are not free to reconsider them now.

Oklahoma Tax, 481 U.S. at 464. By contrast, Section 11501(b)(1) does not clearly say that railroads may go beyond challenging the application of a state's reasonable valuation method and urge the district court to reject that methodology in favor of another.

CSXT also argues that "Congress has already balanced federal and state interests in § 11501(b)(1)." Pet. Brief, p. 42. That argument proves too much and would swallow the "clear statement" rule this Court has long

applied, for Congress can always be said to have balanced federal and state interests when it enacts legislation affecting the states. The real question is where that balance has been struck. Although Congress included some provisions to address specific issues raised by the states during hearings on the statute and its predecessor versions – like the 5% threshold set out in § 11501(c)[9] – these did not eliminate federalism entirely as a factor in ascertaining the Act's proper scope. For example, CSXT points to the fact that the 4-R Act did not become effective until three years after its enactment as proof that Congress rejected the federalism concerns that this case presents. Pet. Brief, p. 43 ("[I]n order to give the States an opportunity to bring their taxation practices into compliance, Congress granted a grace period of three years before § 11501 went into effect.") The provision construed in *ACF Industries* was subject to the same delayed effective date, and this gave the Court no pause in concluding

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[9] George Kinnear, Director of the Washington Department of Revenue, proposed the 5% tolerance factor to accommodate one State practice unrelated to discrimination against common carriers: "Another example is to be found in the Tolerance factors built into the ratio studies of various States. Oregon has one now and Washington is presently considering the establishment of such a Tolerance. If, under this practice, a given assessor claims to be assessing at 25% of full value and the conclusion of the State Ratio Study results in a difference of not more than 5% (i.e., 23.75% ratio), the state will concede a possible error in judgment and officially conclude the assessor's claimed ratio to be correct. Yet in the case of State assessed properties, such as common carriers, this difference in finding in the allowance of the Tolerance could be claimed as a base for challenging the tax assessments and levies of the railroads." *State Tax Discrimination Against Interstate Carrier Property: Hearing On S. 2289 Before the Subcomm. On Surface Transportation of the S. Comm. On Commerce*, 91st Cong. 100 (1969) (statement of George Kinnear, Director, Washington Department of Revenue).

that "[p]rinciples of federalism support, in fact compel, our view [of the statute's reach]." *ACF Industries*, 510 U.S. at 345.

Despite CSXT's suggestion to the contrary, *see, e.g.*, Pet. Brief. p. 2 ("the valuation approaches at issue here are simply standard appraisal tools"), a state's decision on how best to value railroad property involves legitimate policy choices to which principles of federalism demand deference. *See Louisville & Nashville R.R. Co. v. Dep't of Revenue*, 736 F.2d 1495, 1498 (11th Cir. 1984) ("These arguments broach delicate issues implicating the state's traditional authority to select methods of valuation.") A state's decision to use a summation approach instead of the unit rule is quintessentially a matter of policy, and Congress could not have contemplated that the courts would second guess that selection based on competing expert testimony about which economic theory supposedly estimates "true market value" more accurately for rail property. To calculate a railroad's unit value, a state might, for example, choose to use a direct capitalization method instead of a DCF analysis because of "the state's limited resources and the tremendous time pressures under which the state's appraisals must be prepared." *Union Pacific*, 716 F. Supp. at 557. *See also* Jt. App. 255 ("Time pressures and limited resources . . . may compel a state to choose a simple valuation methodology rather than a complicated one."); *Bair*, 815 F. Supp. at 1229 n.4 ("[A] DCF requires much research and is complex. It is doubtful [a] DCF would be practicable for the state to employ to value all railroads in its jurisdiction every two years.") A state might prefer a method, like the stock-and-debt approach, that is based on historical and market data readily available to the state and the affected taxpayers,

both for its relative ease of application and its transparency. The Eleventh Circuit properly took these policy concerns into consideration when refusing, as this Court did in *ACF Industries*, "to extend the statute beyond its evident scope." Jt. App. 255. *See also Chesapeake Western*, 938 F.2d at 531 ("[w]hile [Section 11501] was passed as an express exception to the policy of non-interference [in state tax decisions], we are not inclined to disregard this general policy in areas where [Section 11501] does not plainly authorize such an exception."); *Union Pacific*, 716 F. Supp. at 552 ("The question . . . is whether the state is free to choose among accepted valuation methods or whether the 4R Act compels the use of one particular method. . . . [T]his court has found nothing in the 4R Act itself . . . that requires this court to make the state apply a particular valuation methodology."); *Bair*, 815 F. Supp. at 1228-29 (same).

II. Section 11501(b)(1) Does Not "Plainly" Allow A Railroad To Challenge The True Market Value Of Its Assets Determined By Correctly Applying A Reasonable Valuation Methodology Chosen By The State

Much of CSXT's brief is devoted to the theme that Section 11501(b)(1) "plainly" permits a railroad to challenge the true market value of its assets determined under a correctly applied, reasonable valuation method chosen by the state. But there is more than one way to estimate the value of railroad property, and Section 11501(b)(1) – even if viewed in isolation – does not "plainly" allow railroads to subject a state to a battle of expert witnesses over whether the railroad has a method that is "better" than the state's, turning the district court into a federal

board of equalization. The provisions in subsection (c) on how to calculate the ratio of assessed value to true market value of other commercial and industrial property also support the Eleventh Circuit's reading of Section 11501(b)(1).

A. The "true market value" of railroad property can be estimated in more than one way

Valuation is not a matter of mathematics. *Hamm v. Comm'r*, 325 F.2d 934, 940 (8th Cir. 1963). Rather, "[t]he concept of true market value is inherently an approximation, in some sense a fiction, since there is no such thing as a perfect market." *Chesapeake Western*, 938 F.2d at 531. "A market deals with ranges of value rather than one set value," *Southern Pac. Transp. Co. v. Dep't of Revenue*, 1989 Ore. Tax LEXIS 1, **42, and federal courts therefore have recognized that the "true market value" of railroad property can be estimated in more than one way.

During the congressional hearings eventually leading to the passage of the 4-R Act, a railroad industry representative acknowledged that "[i]n the hundred-year history of railroad taxation, the practice of valuing railroads for tax purposes has reached a substantial degree of refinement." *Tax Assessments On Common Carrier Property: Hearing on H.R. 736 and H.R. 10169 Before the Subcomm. On Transportation and Aeronautics of the H. Comm. On Interstate and Foreign Commerce*, 88th Cong. 18 (1964) (statement of James N. Ogden, Vice President of the Gulf, Mobile & Ohio Railroad). Indeed, if a state has decided to use the unit rule in estimating the value of a railroad's property in its jurisdiction, there are multiple methods from which to choose for arriving at a unit value, including

the stock-and-debt, DCF, and market multiples approaches used by the State in this case. *See Discriminatory Taxation of Common Carriers: Hearings on S. 927 Before the Subcomm. on Surface Transportation of the S. Comm. on Commerce*, 90th Cong. 66 (1967) ("Highly refined techniques exist for measuring railroad values using such techniques as capitalizing railroad operating income, using the market values of stocks and bonds, and determining depreciated reproduction costs.") (statement of Rolf A. Weil, President, Roosevelt University). Each such method, when properly applied, will give an estimate of "true market value," and Section 11501(b)(1) does not "plainly" allow a railroad to dispute true market value determined by the state in that way by urging the district court to use a different method to estimate value. As noted by the Fourth Circuit, "[t]here is no absolute way to test the assertions of competing valuations or competing claims of correspondence to 'true market value,' if such a thing exists in the order of things." *Chesapeake Western*, 938 F.2d at 532 (quoting *Union Pacific*, 716 F. Supp. at 553). The Fourth Circuit embraced this "rich explanation of the problem":

> [V]aluation is an art, not a science. . . . Absent a miracle of time, place, and circumstance – willing buyer, willing seller, high noon, January 1, 1984, for example – true market value for the purposes of ad valorem taxation is always an estimate, always an expression of judgment, always a result built on a foundation of suppositions about knowledgeable and willing buyers and sellers endowed with money and desire, whose desires are said to converge in a dollar description of the asset.

Chesapeake Western, 938 F.2d at 532 (quoting *Union Pacific*, 716 F. Supp. at 554).

CSXT's arguments are based in part on Congress' use of the word "true" in the statutory term "true market value," which CSXT takes to mean a *single best* estimate of the railroad property's value. *See* Pet. Brief, pp. 30-31 ("Congress's charge to a district court . . . to determine the '*true* market value' of railroad property . . . requires an independent and neutral finding by the district court of the market value of the property that is 'true' based on the available evidence presented by the parties."); *see also* Brief of Amicus Curiae Association of American Railroads In Support of Petitioner ("AAR Amicus Brief") p. 16 ("Congress . . . meant what they said: 'true' means true. . . .") But the word "true" cannot bear the weight that CSXT and its supporters place upon it. As explained by the railroad proponents of this legislation:

> "True market value" is the goal generally sought by all tax assessors either as the assessment figure or as a starting point from which final assessments of less than "true market value" may be computed. In an authoritative treatise published by the National Association of Tax Administrators, the following statement appears:
>
> "The statutes of the several States prescribing the value standard for tax purposes use such terms as 'fair market value,' 'fair cash value,' 'full market value,' and the like. All of these terms are synonymous: they mean nothing more and nothing less than what we mean in this report by the term 'market value' or the word 'value' without a qualifying adjective."

Discriminatory Taxation of Common Carriers: Hearings on S. 927 Before the Subcomm. on Surface Transportation of the S. Comm. on Commerce, 90th Cong. 29 (1967) (statement of James A. Ogden, Vice President and General Counsel, Gulf, Mobile & Ohio Railroad). Congress accepted this definition. S. Rep. No. 90-1483, at 10 (1968); *id.* at App. B. In other words, Congress could just have easily referred to the ratio of assessed value to "fair" market value, and it hardly is "unfair" to compute market value by correctly applying a reasonable valuation method.

CSXT argues that a railroad should not be limited to proving its "true market value" under a state's chosen valuation methodology because "ascertaining true market value for any property *requires* . . . taking into account *all* the pertinent factors that influence market value." Pet. Brief, pp. 8-9 (emphasis added). Petitioner does not truly believe that statement, because it elsewhere asserts that the stock-and-debt method should *not* be used to derive a railroad's unit value, even though this Court long ago accepted that approach. As this Court stated in *State Railroad Tax Cases*, 92 U.S. 575, 605 (1876):

> [W]hen you have ascertained the current cash value of the whole funded debt, and the current cash value of the entire number of shares, you have by the action of those who above all others can best estimate, ascertained the true value of the road, all its property, its capitalized stock and its franchises; for these are all represented by the value of its bonded debt and the shares of its capital stock.

See also Adams Express Co. v. Ohio State Auditor, 165 U.S. 194, 222 (1897) ("The value which property bears in the market, the amount for which its stock can be bought

and sold, is the real value."); S. Rep. No. 87-445, at 456 (1961) ("Doyle Report") ("Next to capitalization of earnings, as a means to determine carrier system value, the market value of stock and debt has widest acceptance as an evidence of value.") CSXT appears to believe that the 4-R Act essentially overruled this Court's prior decisions, because it argues that it should be allowed "to prove in court that a stock-and-debt method cannot reliably estimate 'true market value.'" Pet. Brief, p. 32.

In any event, it is incorrect to claim that a railroad, in order to prove the true market value of its property, must be free to derive that value under whatever approach it thinks is best, even if the taxing jurisdiction has adopted a different valuation method from within the range of reasonable options available. Even the Uniform Standards of Professional Appraisal Practice ("USPAP"), the generally accepted standards for professional appraisal practice in North America, acknowledges that its provisions can be "void and of no force and effect" in a particular appraisal assignment because of contrary state law or public policy. USPAP, "Jurisdictional Exception" (2006 ed.). By refusing to afford the states any latitude in choosing appropriate methods for estimating the value of property within their jurisdictions, CSXT would turn the district courts into federal boards of equalization required to oversee protracted, complicated battles between expert witnesses over whose method is "best."

During the oral argument in *Oklahoma Tax* the following exchange occurred between the Court and counsel for the railroad:

> Question: Will you concede then that all the federal court would have to do is use whatever

> methodology the state used, assuming that was a reasonable methodology?
>
> Mrs. Christian: We think the door would have to be open for the railroad to challenge a particular methodology as not being a reasonable methodology.
>
> Question: Right.
>
> Mrs. Christian: But given that caveat, yes his role would be to determine on the basis of the evidence before him, which would include the evidence of the state's expert and the railroad's expert as to whether these methodologies have been properly applied.[10]

Transcript of Oral Argument, *Burlington N. R.R. Co. v. Okla. Tax Comm'n*, 481 U.S. 454 (No. 86-337), 1987 U.S. TRANS LEXIS 61 at *12. The Deputy Solicitor General, representing the United States as an amicus supporting the railroad, was asked the same question:

> Question: Do you agree with Mrs. Christian as to what has to be accepted? That the federal court has to accept any manner of assessment adopted by [the] state, methodology adopted by the state if it's a reasonable one?
>
> Mr. Lauber: I would agree that there are probably some methodologies like [undepreciated] book cost, that simply would be ridiculous . . .

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[10] Counsel later tried to withdraw that concession, stating "Justice Scalia, I apologize if I said . . . the court would have to accept the [state's] methodology. Certainly the railroad's witnesses would be free to state that they believe other methodologies were preferable."

> Question: I understand. But more in the range of reasonable ones, the federal court has to accept whatever the state applies?
>
> Mr. Lauber: I would say it ought to accept it. It should listen to arguments that they're out of line, but ought to normally accept the state's methodology.

Id. at *27. That response echoed the Solicitor General's amicus brief in that case, which stated that Section 11501(b)(1) applied:

> to overvaluations that result from an assessment rule or methodology that – either on its face or as applied – *systematically* determines excessive values for rail property. On the other hand, if a railroad, like any other state taxpayer, asserts only that the state made an error in reaching an excessively high value for its property, no relief for that overvaluation claim would be available under [the statute].

Brief for the United States as Amicus Curiae Supporting Petitioner, *Oklahoma Tax*, No. 86-337, p. 25 n.14 (Dec. 12, 1986) (emphasis added). These statements demonstrate that Section 11501(b)(1) is anything but plain on the question presented here.

B. Section 11501(c)'s provisions on how to compute the ratio of assessed value to true market value of other commercial and industrial property support the Eleventh Circuit's reading of Section 11501(b)(1)

CSXT asserts that "subsection (c)'s provisions allowing proof of the market values of other commercial and industrial property underscore that the district court is to

determine the true market value of property independently, regardless of what methods the state appraiser employs." Pet. Brief, p. 34.[11] In fact, those provisions support the Eleventh Circuit's holding. Section 11501(c) provides for the use of a "sales assessment ratio study," which compares the sales prices of a sample of recently sold properties with their assessed values. *See Oklahoma Tax*, 481 U.S. at 461-62; S. Rep. No. 90-1483, at 23-24 (1968). This calculation is possible only because for non-rail property there is an ongoing market that produces actual sales prices. By contrast, the 4-R Act prescribes no method for calculating the ratio of assessed value to market value for rail property. While this omission does not indicate that the value of "[rail] property may not be proved *at all*," *Oklahoma Tax*, 481 U.S. at 463 (footnote omitted and emphasis added), it does support the conclusion that Congress did not mean to take away the states' right to choose for themselves appropriate methods for estimating the value of railroad property in their jurisdictions.

In addition, ascertaining the ratio of assessed value to true market value for "all other commercial and industrial property in the same assessment jurisdiction" is not the same as the individualized inquiry involving a particular railroad's ratio. The first task is designed to see how the taxing authorities have treated a "hypothetical 'average'

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[11] CSXT also points to the provision in subsection (c) that "[t]he burden of proof in determining assessed value and true market value is governed by State law," arguing that Congress would not have required railroads to prove their value but then limited them to adducing evidence that was relevant under the State's chosen valuation methodology. Pet. Brief, p. 34. However, CSXT does not explain why it thinks that is a logical disconnect.

taxpayer" in the assessment jurisdiction. S. Rep. No. 91-630, at 26 (1969).

> In making this comparison, the bill contemplates the relationship between a common carrier's property and that of the "average" taxpayer in the taxing district. However, the word "average" has a precise arithmetical connotation which makes it unsuitable in this context.
>
> For simplicity, therefore, the phrase "all other property in the taxing district"[12] has been used as the equivalent of the property of the "average" taxpayer there. Thus the words "all other property" are to be construed as meaning property in the aggregate, and not individually as separate parcels or kinds of property.

Id. Accord Arizona v. Atchison, Topeka & Santa Fe R.R. Co., 656 F.2d 398, 404 (9th Cir. 1981) ("The legislative history is clear that Congress understood the term 'all other [commercial and industrial] property' to mean property in the aggregate.") Looking at other commercial and industrial property "in the aggregate" could require examining hundreds or thousands of such properties, and it could be extremely difficult (if not impossible) to determine what method local assessors used to value each such property and then to calculate its "true market value" in similar fashion. By allowing sales ratio studies, Congress opted for the most efficient way to compute an assessment ratio for what was intended, at the end of the day, to represent only a hypothetical "average" taxpayer in the comparison group. Congress did not thereby imply that

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[12] Before the statute was enacted the comparison group was narrowed to "all other commercial and industrial property."

railroads could freely attack a state's reasonable method for estimating the true market value of the railroads' property in that jurisdiction.

III. The 4-R Act's Legislative History Confirms That Congress Did Not Intend For Courts To Displace A State's Choice Of An Appropriate Method For Valuing Railroad Property

Courts that have considered the 4-R Act's legislative history have found that this history, while it does not deal extensively with the issue presented in this case, confirms that Congress did not intend to displace a state's legitimate policy choices when selecting an appropriate method for valuing railroad property. Jt. App. 210, 211, 257; *Chesapeake Western*, 938 F.2d at 531 ("the history that does exist suggests that Congress did not intend for courts to displace the state's policy choice about what constitutes the best method for determining true market value of railroad land."); *Union Pacific*, 716 F. Supp. at 553 ("the legislation history suggests that the statute was not meant to dictate a state's choice of methodology, at least as long as the methodology chosen had a rational basis and was not chosen for a discriminatory purpose."); *Bair*, 815 F. Supp. at 1229 (same). During the hearings leading eventually to the 4-R Act's adoption, representatives of the railroads were asked what effect the proposed legislation would have on state valuation methodologies.[13] These

[13] "With the passage of the 4R Act, Congress capped a seventeen-year effort to equalize railroad property taxes. . . . The legislative history of nearly identical antecedent proposals is unquestionably relevant and material for a complete understanding of the text before the court." *Louisville & Nashville R.R. Co. v. Dep't of Revenue*, 736 F.2d

(Continued on following page)

representatives advised Congress that the railroads generally were satisfied with the methods that states employed when valuing their property. James N. Ogden, Vice President of the Gulf, Mobile & Ohio Railroad, appearing on behalf of the Association of American Railroads ("AAR"), stated:

> The principal problem in the matter of railroad assessments is not one of how to value a railroad. In the hundred-year history of railroad taxation, the practice of valuing railroads for tax purposes has reached a substantial degree of refinement. . . . The real problem is to determine how much of the valuation that has been found should be assessed, which, in turn, depends upon how much of the valuation of other property is assessed. In other words, the problem is how to get the tax assessors in the several States to equalize the railroad's assessment with that of other property in the same taxing district.

Tax Assessments On Common Carrier Property: Hearing on H.R. 736 and H.R. 10169 Before the Subcomm. On Transportation and Aeronautics of the H. Comm. On Interstate and Foreign Commerce, 88th Cong. 18-19 (1964). *See generally Discriminatory Taxation of Common Carriers: Hearings on S. 927 Before the Subcomm. on Surface Transportation of the S. Comm. on Commerce*, 90th Cong. 66 (1967) ("Highly refined techniques exist for measuring railroad values using such techniques as capitalizing railroad operating income, using the market values of

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1495, 1498 n.6 (11th Cir. 1984). *Accord Arizona v. Atchison, Topeka & Santa Fe R.R. Co.*, 656 F.2d 398, 404 n.6 (9th Cir. 1981).

stocks and bonds, and determining depreciated reproduction costs. These valuation methods certainly produce results which provide sufficiently accurate measures of value to make valid comparisons [with other properties' values]") (statement of Rolf A. Weil, President, Roosevelt University). Philip M. Lanier, Vice President of the Louisville & Nashville Railroad, also appearing on behalf of the AAR, was asked to describe Wyoming's valuation procedures:

> It is what we call a three factor formula. The factors of the formula are the net railroad operating income over the preceding 3 years capitalized at 8 ¼ percent; 1 year stock and debt, that is . . . the market value of the stock and debt; and the replacement cost of the property less depreciation with allowance for obsolescence.
>
> . . . These three factors would be computed and averaged and the resulting value – this gives you the system value of the whole railroad. . . .

State Tax Discrimination Against Interstate Carrier Property: Hearing On S. 2289 Before the Subcomm. On Surface Transportation of the S. Comm. On Commerce, 91st Cong. 38 (1969). Mr. Lanier then was asked "[i]s this same formula – this same three-factor formula in use . . . throughout the country, or is this only the way it is done in Wyoming," to which Mr. Lanier replied, "[t]he formula varies from State to State and we are not dealing with the valuation question. This is not our problem." *Id.* at 39. In a subsequent hearing, Mr. Lanier also stated that "[t]he standards and methods of valuation that any State wishes to use would be totally unaffected by this legislation." *Common and Contract Carrier State Property Tax Discrimination: Hearing on H.R. 16245 Before the Subcomm.*

On Transportation and Aeronautics of the H. Comm. On Interstate and Foreign Commerce, 91st Cong. 138 (1970) (statement of Philip M. Lanier, Vice President, Louisville & Nashville Railroad).

What the railroads and their supporters had to say about the Act's meaning was taken seriously by Congress and should be given weight here because the railroad industry was in effect the primary sponsor of the legislation. In 1961, the Association of American Railroads had proposed to a special congressional study group an anti-discrimination tax law with many of the essential provisions contained in what became the 4-R Act. *See* S. Rep. No. 87-445, at 465 (1961) (suggested legislation giving federal courts jurisdiction to enjoin "[t]he assessment, for the purposes of a property tax levied by any taxing district, of property owned or used by any common carrier engaged in interstate commerce at a value which bears a higher ratio to the true market value of such property than the assessed value of all other property in the taxing district subject to the same property tax levy bears to the true market value of all such property.") Thereafter, in 1967, the railroads told members of Congress that the proposed legislation that was then pending in the Senate:

> does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves. It merely provides a single standard against which all affected assessments must be measured in order to determine their relationship to each other. It is not a standard for determining value; it is a standard to which values that have already been determined must be compared.

Discriminatory Taxation Of Common Carriers: Hearings on S. 927 Before the Subcomm. On Surface Transportation of the S. Comm. On Commerce, 90th Cong. 29 (1967) (statement of James N. Ogden, Vice President, Gulf, Mobile & Ohio Railroad). Virtually identical language subsequently appeared in S. Rep. No. 90-1483, at App. B (1968) as part of the Senate committee's explanation of how the proposed legislation was meant to apply.

CSXT contends that the Eleventh Circuit has "misread" that record. Pet. Brief, p. 49. According to CSXT, testimony before Congress that the proposed legislation "does not suggest or require a State to change its assessment standards [or] assessment practices" meant simply that "States could continue to use whatever methods they liked" even if a district court rejected those methods and found that true market value should be computed in another way, because "courts could not issue injunctions dictating what valuation and assessment methods States must use going forward in imposing taxes." Pet. Brief, p. 50. That is a pinched reading of what the railroads told Congress when trying to get their legislation passed and an exceedingly strange view of how litigation works in the real world. If fair market values that the state calculates for railroads using valid, properly applied methodologies can successfully be attacked in federal court through the use of different methodologies, the state – unless it wishes constantly to be engaged in expensive, protracted litigation – will have no real choice but to change its assessment practices. The Solicitor General counters by saying that "some States do not . . . base assessments on true or fair market value." Brief of the United States as Amicus

Curiae Supporting Petitioner ("U.S. Brief"), p. 17.[14] But Congress adopted the term "true market value" with the understanding that "'[t]rue market value' is the goal generally sought by all tax assessors either as the assessment figure or as a starting point from which final assessments of less than true market value may be computed." S. Rep. No. 90-1483, at App. B (1968).[15] *See also* S. Rep. No. 87-445, at 455 ("Different methods are employed by the various States to find value, but for ad valorem taxation the goal is to find market value.") If a taxing jurisdiction nevertheless were to assess railroad property according to an entirely different standard, that fact would mean only that whatever valuation methodology the tax officials used – being designed to arrive at something other than "true market value" – could not factor into the district court's decision.

CSXT maintains that "[t]hroughout the debate on proposed legislation, it was well understood that allowing railroads to attack discriminatory taxes . . . would entail judicial scrutiny of state valuation procedures." Pet. Brief, pp. 47-48. No one questions that in an action under Section 11501(b)(1) district courts may thoroughly examine whether a state has applied its particular valuation

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[14] CSXT disagrees. *See* Pet. Brief, p. 7 ("In some states the assessed value is equal to the market value; in others assessed value is a specified percentage of the market value. . . . In *every* jurisdiction assessing an ad valorem tax, therefore, the market value of the subject property directly affects the total amount of the tax.") (emphasis added).

[15] In fact, that is precisely what the railroads told Congress. *Discriminatory Taxation of Common Carriers: Hearings on S. 927 Before the Subcomm. on Surface Transportation of the S. Comm. on Commerce*, 90th Cong. 29 (1967) (statement of James A. Ogden, Vice President and General Counsel, Gulf, Mobile & Ohio Railroad).

method correctly, and the district court did so in this case.[16] But in advocating its much more expansive reading of the statute, CSXT looks to comments made during the legislative debates by opponents of the legislation. *Id.* at 48. This Court has said that such "statements are entitled to little, if any, weight," *Selective Service System v. Minnesota Public Interest Research Group*, 468 U.S. 841, 855 n.15 (1984), because "[i]n their zeal to defeat a bill, [its opponents] understandably tend to overstate its reach." *Nat'l Woodwork Mfrs. Ass'n v. NLRB*, 386 U.S. 612, 639-40 (1967). *Compare State Tax Discrimination Against Interstate Carrier Property: Hearing On S. 2289 Before the Subcomm. On Surface Transportation of the S. Comm. On Commerce*, 91st Cong. 80 (1969) ("Under the language of the bill as presently drafted, it is my opinion that a railroad would be entitled to [an assessment at the lowest percentage of value applicable to any other class of property]") (statement of Charles F. Conlon, Executive Secretary, National Association of Tax Administrators) *with Arizona v. Atchison, Topeka & Santa Fe R.R. Co.*, 656 F.2d 398, 404 (9th Cir. 1981) ("The language was not meant to permit railroads to demand the same treatment as those holding property with the lowest assessment ratio"). CSXT also relies on a suggestion by one state taxing official, not taken by Congress, to define "true market value" as "that true market value finally determined in accordance with

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[16] The district court carefully considered and rejected CSXT's challenges to the "comparability" of the Class I railroads that Mr. Dickerson selected to estimate CSXT's unit value under the "market multiples" method, his stock-and-debt method, virtually every assumption made by Mr. Dickerson in applying the DCF method (including the terminal growth rate and projected operating ratio in year 2011), and Mr. Dickerson's "leased equipment" adjustment. Jt. App. 217-229.

state statutory procedures." Pet. Brief, p. 48; *State Tax Discrimination Against Interstate Carrier Property: Hearing On S. 2289 Before the Subcomm. On Surface Transportation of the S. Comm. On Commerce*, 91st Cong. 102 (1969) (statement of George Kinnear, Director, Washington Department of Revenue). But Congress easily could have felt that such a provision would sweep too broadly and preclude any review of a state's value determination as long as it had been made in compliance with all state procedural requirements – such as timeliness, notice to the taxpayer, etc. – even if it were based on a misapplication of that state's particular valuation methodology.

CSXT claims that "[a]s documented in congressional studies and hearings, the valuation methods and practices that the States employed were a major source of discrimination against the railroads." Pet. Brief, p. 21. In reality, from all the discussions about the unit rule, different apportionment formulas, and methods such as capitalized income and stock-and-debt, the only real concern to emerge involved what was described as "outmoded" or "outdated" procedures. *See, e.g.*, S. Rep. No. 87-445, 448 (1961) ("discrimination results . . . by virtue of outmoded assessing procedures.") *id.* at 451 (reference to "outdated" procedures). No one questioned the states' right to value railroad property using reasonable, correctly applied methods.

IV. This Court's Decisions Approving The Unit Rule And Formulary Apportionment Recognize That States Are Entitled To Latitude In Estimating The Value Of Taxable Property Within Their Jurisdiction

In determining how best to estimate the "true market value" of railroad property within its jurisdiction, a state must first choose between the unit rule and summation approach and, if the former, then select an apportionment formula for assigning a portion of the railroad's unit value to the state. This Court's decisions upholding the unit rule and formulary apportionment recognize that states are entitled to latitude in this regard. CSXT, on the other hand, would not afford the states any leeway in estimating the value of railroad property within their jurisdictions when they are sued under Section 11501.

"[T]he 'unit rule' developed in the late nineteenth century for apportioning property values of railroad, telegraph, and express companies to state or local taxing jurisdictions." 1 Jerome R. Hellerstein & Walter Hellerstein, *State Taxation* ¶ 8.07[1] (3d. ed. 2000).

> To ascertain the value of a company's property that was properly attributable to the taxing jurisdiction, states and localities would determine the value of the entire operating system and then assign to the state or locality a proportion of the system value based on the ratio of the amount of some identifiable factor within the state to the amount of such factor in the entire system.

Id. See also S. Rep. No. 87-445, at 455 (1961) ("The major procedural steps in the assessment of railroads and pipelines [include]: (a) Determination of the value of the property as a unit; [and] (b) Allocation of the system value

to the State"); 2 James C. Bombright, *The Valuation Of Property* 633 (1st ed. 1937) ("Under [the unit] rule, in its more thoroughgoing form, the entire enterprise is first valued as a unit, some 'fair share' of this value (perhaps after the deduction of certain asset values deemed inappropriate for allocation) being attributed to the particular state or district that is imposing the tax.").[17] Well over one hundred years ago, this Court held that a state was free to choose this method for estimating the taxable value of property within its jurisdiction:

> It is further objected that the railroad track, capital stock, and franchise is not assessed in each county where it lies according to its value there, but according to an aggregate value of the whole, on which each county, city, and town collects taxes according to the length of the track within its limits.
>
> . . . But, as we have already said, a railroad must be regarded for many, indeed for most purposes, as a unit. The track of the road is but one track from one end of it to the other, and, except in its use as one track is of little value. . . . It may well be doubted whether any better mode of determining the value of that portion of the track within any one county has been devised than to ascertain the value of the whole road,

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[17] 2 James C. Bombright, *The Valuation Of Property* at 633 n.1 ("The term 'unit rule' is often used in its broadest sense, to denote any assessment . . . under which the value of . . . property located within a specific geographical area is taken to be equal to a certain share of the value of . . . a larger aggregate of property, of which the former property is an integral part. When used in this broad sense, the unit rule does not necessarily require a valuation of an entire business enterprise.")

> and apportion the value within the county by its relative length to the whole.

State Railroad Tax Cases, 92 U.S. 575, 608 (1875).[18] At the same time, the Court said that this method was permissible rather than mandatory, and at least one state supreme court has held that state law did not allow the unit rule. *See County Bd. of Arlington County v. Commonwealth of Va. Dep't of Tax'n*, 240 Va. 108, 112 (1990) ("Generally, in assessing real estate for local taxation, the commissioner should seek to determine its fair market value by a consideration of its highest and best use in its *particular* location. The commissioner testified, however, that his appraisals do not reflect the fair market value of Potomac Yard in its particular location, but do reflect its fair market value as a part of the railroad unit.") (internal citations omitted); *Chesapeake Western*, 938 F.2d at 529-30 ("The Virginia Supreme Court ... held that the unit method constituted a business tax rather than a real property tax and it struck down its use as unconstitutional.")

It is impossible to coax from the 4-R Act any intimation that Congress intended to limit states' latitude in deciding to adopt either the unit rule or the summation approach for estimating the "true market value" of railroad assets within their jurisdictions. Although CSXT is careful not to tip its hand too obviously in this regard,

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[18] "While the Court's articulation of the unit rule [in *State Railroad Tax Cases*] was addressed to the apportionment of the railroad's property among counties rather than among states, the Court subsequently applied the same principles to disputes [that] involved interstate values." 1 Jerome R. Hellerstein & Walter Hellerstein, *State Taxation* ¶ 8.05 n.164.

accepting the company's arguments would make even that most fundamental methodological choice fair game under Section 11501(b)(1) any time a railroad thinks that the approach not selected by the state is "better." *See* Pet. Brief, p. 32 ("under the Eleventh Circuit's rule ... [r]ailroads would be unable to present their own, better evidence of value"); *id.* at 28 ("Neither the value of the property nor the methodology for determining that value may be altered by legislative policy.") Indeed, the railroads launched just such an attack in *Chesapeake Western*, urging the Fourth Circuit "not only to reject Virginia's inventory and summation approach but also to dictate to Virginia the specific valuation method that [the railroads alleged] produces the 'correct' market value," which they contended in that case was the unit rule. *Chesapeake Western*, 938 F.2d at 532 n.4. CSXT has said that *Chesapeake Western* was "wrongly decided" in favor of the state, leaving "a gaping loophole in Congress' prohibition of discriminatory valuation of railroad property." COA Reply Brief of Appellant, p. 11.

States also must select methods for apportioning a railroad's total unit value. "Apportionment, under which the measure of a tax is divided by formula, is based on the use of selected factors for attributing the tax base to the states in which the taxpayer employs its property or carries on its activity." *State Taxation*, ¶ 8.05. *See, e.g.*, S. Rep. No. 87-445, at 457 (1961) ("Factors used to apportion to each State its proper share of the system value include: traffic units, gross earnings, car mileage, transportation train-miles, [and] miles operated"). "[T]he States have been permitted considerable latitude in devising formulas to measure the value of tangible property located within their borders," *Norfolk & Western Ry. Co. v. Missouri State Tax Comm'n*, 390 U.S. 317, 324 (1968), even when "it could

not be demonstrated that the results they yielded were *precise* evaluations of assets located within the taxing State." *Id.* (emphasis added). *See also Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 274 (1978) ("the States have wide latitude in the selection of apportionment formulas and [the result] . . . will only be disturbed when the taxpayer has proved by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportions to the business transacted . . . in that State' or has 'led to a grossly distorted result') (quoting *Hans Rees' Sons, Inc. v. North Carolina*, 283 U.S. 123, 135 (1931) and *Norfolk Western*, 390 U.S. at 326). CSXT would deny the states any latitude in estimating the "true market value" of railroad property within their jurisdictions when sued under Section 11501(b)(1).

V. The Distinction Between A Valuation "Method" And Its "Application" Has Proved Workable In Practice

CSXT did not seek review of the Eleventh Circuit's decision upholding the district court's finding that the railroad's appraiser used a valuation methodology different from the State's. Consequently, if this Court holds that Section 11501(b)(1) limited CSXT to challenging the application of the State's valuation methodology, the Eleventh Circuit should be affirmed. However, to support its claim that this Court should not recognize *any* distinction whatsoever between states' valuation "methods" and their "application," CSXT says that no workable line can be drawn between the two. While the Court in *Oklahoma Tax* did not resolve the question whether a state's valuation methodology may be disputed under Section 11501(b)(1), it still noted a difference between a challenge

to "the valuation methodology employed by [a state]" and "the application of that methodology." 481 U.S. at 463 n.5. That statement hardly suggests that this Court considered the distinction meaningless.

The Eleventh Circuit concluded that a State's valuation "methodology" consists of "all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be." Jt. App. 260. *Cf. Oklahoma Tax*, 481 U.S. at 463 n.5 (describing the issue as "whether a railroad may[] ... challenge ... the appropriateness of the *accounting methods* by which the State determined the railroad's value, or is instead restricted to challenging the *factual determinations* to which the State's preferred accounting methods were applied.") One district court has differentiated "between formulas that are used in the various methods of appraising and the specific numbers, percentages, types of property and any other matter that the individual appraisers use to make the formula applicable to the specific appraisal in question." *Bair*, 815 F. Supp. at 1229 (rejecting the railroad's argument that state should have determined the company's unit value under a DCF rather than stock-and-debt and capitalized income approaches). In *Chesapeake Western*, the Fourth Circuit did not articulate a test but simply recognized the distinction between "methods" and "applications" and then found that the railroads' effort to convince the court "to reject Virginia's inventory and summation approach ... and dictate [the unit rule] to Virginia" was a dispute about "methods" that the court could not consider. *Chesapeake Western*, 938 F.2d at 532 n.4. Later, in *Richmond, Fredericksburg & Potomac R.R. Co. v. Forst*, 4 F.3d 244, 248-249 (4th Cir. 1993), the Fourth Circuit held that the railroad had sufficiently alleged that

the state misapplied its "across the fence" methodology by failing to make adjustments required under that method to account for differences in a property's size, shape, topography, accessibility and additional physical features.

The Solicitor General concedes that "when a State is making the initial determination whether to use the unit rule or the summation method to value railroad or other property, it may be fair to say that the choice is purely one of methodology." U.S. Brief, p. 21. Nor, for example, is there a plausible argument that the stock-and-debt method is just a different "application" of a DCF method. To be sure, there can be closer questions, including the one that the Eleventh Circuit addressed in this case but that CSXT did not appeal. But so far the courts have in practice been able to discern the appropriate line between different "methods" on the one hand and different "applications" of the same method on the other, even though the boundary may not always be perfectly distinct or easily described in the abstract. Petitioner suggests that, in order to avoid any possibility whatsoever of confusion at the margins, the railroads should always be permitted to subject a state's valuation methodology to a battle of expert witnesses over whether it is "better" than any other method a railroad might wish to use – whether the unit rule instead of a summation approach, *see Chesapeake Western*, 938 F.2d at 532 n.4, a DCF instead of a capitalized income method, *see Bair*, 815 F. Supp. at 1227, or any method (presumably) instead of the stock-and-debt approach that this Court approved many years ago. *See* Pet. Brief, p. 32 ("a stock-and-debt method cannot reliably estimate 'true market value.'"). That is a cure that is worse than the alleged disease, turning the district courts into federal boards of equalization, and extending Section 11501(b)(1) beyond its

evident scope, all at the expense of legitimate policy choices that states should be free to make in selecting methods to estimate the taxable value of property within their jurisdiction.

VI. CSXT Is In No Event Entitled To A New Trial

Finally, CSXT says that this case should be "remanded for a new trial." Pet. Brief, p. 50. CSXT does not, however, articulate any reason for that prayer for relief, and there is none. Although the district court concluded after trial that it could not consider the railroad's appraisal in finding CSXT's "true market value," the judge received that appraisal into evidence along with all of the testimony that CSXT offered in support thereof.[19] In fact, CSXT contends that it "argued and proved that its true market value was $6 billion." Pet. Brief, p. 16. The State disagrees with that claim, but it clearly illustrates that, regardless how this Court decides, a "new trial" is not needed.

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[19] The statement on page 2 of CSXT's brief that the Eleventh Circuit "upheld the exclusion of CSXT's expert testimony on the market value of its property" is incorrect.

CONCLUSION

For the reasons above, the Respondents respectfully ask that the decision by the Eleventh Circuit be affirmed.

Respectfully submitted,

THURBERT E. BAKER
Attorney General

WARREN R. CALVERT
Senior Assistant
Attorney General
(*Counsel of Record*
for Respondents)

R. O. LERER
Deputy Attorney General

Attorneys for Respondents

GEORGIA DEPARTMENT OF LAW
40 Capitol Square, S.W.
Atlanta, Georgia 30334-1300
(404) 656-2647

PETER J. CROSSETT
JOHN D. COOK
HISCOCK & BARCLAY, LLP
One Park Place
300 South State Street
Syracuse, New York
13202-2078
(315) 425-2814

71 151 (10) 24

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IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION of the State of Georgia; Bart L. Graham, as Commissioner of Revenue of the State of Georgia; Russell W. Hinton, as State Auditor of the State of Georgia; and Gena L. Abraham, as Director of the Georgia State Properties Commission,

Respondents.

On a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

REPLY BRIEF OF PETITIONER

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
MATTHEW J. WARREN
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Avenue, NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON, BEARMAN, CALDWELL & BERKOWITZ, PC
555 Eleventh Street, NW
(202) 508-3400

Counsel for Petitioner

* Counsel of Record

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REPLY BRIEF

Respondents advance a fundamentally flawed approach to statutory construction. "The starting point for [the] interpretation of a statute is always its language," *Cmty. for Creative Non-Violence* v. *Reid*, 490 U.S. 730, 739 (1989), and courts must "look to the provisions of the whole law, and to its object and policy," *Pilot Life Ins. Co.* v. *Dedeaux*, 481 U.S. 41, 51 (1987) (internal quotation marks omitted). Yet respondents discount the text, surrounding provisions, and policy of section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act" or "the Act"), 49 U.S.C. § 11501, and instead begin with federalism canons. See Resp. Br. 9-18. This misguided approach leads respondents directly to an incorrect interpretation of the 4-R Act.

The "clear-statement" canon of *Gregory* v. *Ashcroft*, 501 U.S. 452 (1991), may be invoked only when the statutory text is ambiguous and "susceptible of two plausible interpretations, one of which would have altered the existing balance of federal and state powers." *Salinas* v. *United States*, 522 U.S. 52, 59-60 (1997). The canon is not a license to rewrite a federal statute to advance state interests that Congress plainly decided must yield to an overriding federal interest. Section 11501 vests the district court with the power to determine the factual question of a railroad's "true market value." Absolutely nothing in the statutory text limits the district court to applying the State's preferred methodologies or restricts the evidence of market value that the court may consider in resolving that factual question. Respondents propose nothing more than to rewrite § 11501(b)(1) in a way that eviscerates the federal discrimination remedy and defeats Congress's purpose. This Court should reject respondents' approach and give the statute its plain meaning.

1. Subsection (b)(1) outlaws various forms of state and local tax discrimination against railroads, including "[a]ssess[ing] rail transportation property at a value that has a higher ratio to the true market value of the rail transportation

property" than the comparable ratio for other commercial and industrial property. 49 U.S.C. § 11501(b)(1). Subsection (b)(1) thus defines "in no uncertain terms" a "precise" federal discrimination standard based on comparison of assessed-to-market value ratios. *Dep't of Revenue of Or.* v. *ACF Indus., Inc.*, 510 U.S. 332, 343 (1994). Accordingly, a district court resolving a (b)(1) discrimination claim must "determine what the 'true market values' are." *Burlington N. R.R.* v. *Okla. Tax Comm'n*, 481 U.S. 454, 461 (1987). The plain meaning of "*the true* market value" of rail transportation property is the *single* value that the district court finds, based on the evidence, best approximates the most probable cash price at which a willing buyer and a willing seller would agree to exchange the property in a competitive market. Petr. Br. 7, 24; Appraisal Inst., *The Appraisal of Real Estate* 22 (12th ed. 2001); *United States* v. *Miller*, 317 U.S. 369, 374 (1943). That single "true market value" becomes the denominator in the ratio used to determine whether the State has imposed a discriminatory tax in violation of subsection (b)(1).

It is axiomatic that undefined statutory terms are to be given their "ordinary meaning." *FMC Corp.* v. *Holliday*, 498 U.S. 52, 57 (1990). Respondents offer no contrary "plausible interpretation[]," *Salinas*, 522 U.S. at 59, of the statutory phrase "the true market value" of rail transportation property. Instead, they ask this Court to import restrictive terms into the statute to limit the district court to finding "the true market value of [rail transportation] assets determined under a correctly applied, reasonable valuation method chosen by the state." Resp. Br. 8, 18. That is exactly the kind of interpretive rewriting of the statute that this Court flatly rejected in *Oklahoma Tax*. There, the respondent state authorities and the court of appeals, in the name of federalism, had respectively construed this statutory phrase to mean "'state determined market value'" or state-determined market value absent proof of intent to discriminate. 481 U.S. at 461-63. This Court rejected those constructions out of hand as "depend[ing] upon the addition of words to a statutory provision

which is complete as it stands. Adoption of [such a] view would require amendment rather than construction of the statute, and it must be rejected here." *Id.* at 463. Respondents' proposed construction fails for the same reason.

2. Furthermore, respondents' rule cannot be reconciled with the statutory requirement that the district court determine "the *true* market value" of rail transportation property, for it would in many instances force the district court to accept a value that in its judgment was patently wrong, so long as the value was calculated by "a correctly applied, reasonable valuation method chosen by the state." Resp. Br. 8, 18. Respondents have abandoned any defense of the Eleventh Circuit's categorical exclusionary rule, in which the district court would have to accept "all nonfactual determinations . . . [of the state appraiser] in constructing a valuation process, regardless of how broad or narrow they may be," JA 259-60, but they never explicate the "reasonable valuation method" standard they have fashioned out of whole cloth. They merely imply that any methods that have been approved by courts at any time in the past are necessarily "appropriate" and "reasonable." Resp. Br. 22, 28.

For example, respondents suggest that because this Court "accepted" the stock-and-debt approach in certain nineteenth-century cases, a district court must use that approach in determining "true market value" if the State relied upon it. *Id.* at 22-23 (citing *State R.R. Tax Cases*, 92 U.S. 575, 605 (1875)). However, the stock-and-debt approach is generally regarded as an unreliable means of calculating property value (and is generally used only as benchmark for testing valuations generated by more reliable techniques). Petr. Br. 10, 32. The stock-and-debt method is particularly unlikely to yield an accurate value in the (b)(1) context, where the property to be valued is not that of the entire publicly traded railroad corporation, but only of "rail transportation property," 49 U.S.C. § 11501(b)(1), which is limited to "property . . . owned or used by a rail carrier providing transportation subject to the

jurisdiction of the [Surface Transportation] Board." *Id.* §§ 11501(a)(3), 10102(1). A number of railroad corporations (like CSXT) are subsidiaries of publicly traded corporations that conduct other lines of business, and thus any computation of "the true market value of rail transportation property" by sole reliance on the stock and debt prices of the parent corporation is likely to be inaccurate, and certainly the choice of that method should not be conclusive as a matter of law.[1]

Indeed, here the stock-and-debt approach yielded a unit value of $12.022 billion, 47% higher than even the inflated figure that Georgia's own appraiser claimed was CSXT's actual unit value. Pet. App. 4a. Nonetheless, under respondents' construction, if the State had chosen that method and "correctly applied" it (*i.e.*, made no computational errors), the district court would be bound to accept that figure as the "true market value" and to use it in applying the subsection (b)(1) discrimination standard—even if the district court were wholly convinced by other evidence or if inherent flaws or biases in this methodology caused the calculated value not to remotely reflect "the true market value" of the rail transporta-

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[1] Respondents' reliance on the *State Railroad Tax Cases* is particularly ironic, given that the issue there was the constitutionality, as applied to a railroad corporation, of a tax on all the capital and franchises of any corporation doing business in the State. 92 U.S. 575, 602-03 (1875). This Court stated that "all [the railroad's] property, its capital stock, and its franchises" were "represented by the value of its bonded debt and of the shares of its capital stock." *Id.* at 605. That decision says nothing about whether the stock-and-debt method would be appropriate to value "rail transportation property" under the limited definition of that term in the 4-R Act. Moreover, in the *State Railroad Cases*, this Court cogently analyzed the shortcomings of the stock-and-debt method, even while declining to find it unconstitutional as employed in the state statute at issue. It recognized that, while the value of a corporation's bonded debt and shares theoretically should reflect the value of its property, in the real world this calculation might not reflect the actual value of the railroad's property. *See id.* at 605. For instance, a railroad with a stock and debt value of zero could still possess real property with a value that could be taxed. *See id.* at 605-06.

tion property. The statute cannot bear the meaning respondents would give it.

Respondents' "reasonable valuation method" standard would similarly force district courts to use replacement cost methods, if chosen by the State. Replacement cost methods were accepted by courts in the past, but nevertheless have long been recognized as an inaccurate measure of value because the difficulty of calculating all forms of depreciation and economic obsolescence makes it a poor fit for modern railroads. See S. Rep. No. 87-445, at 456-57 (1961). As the Solicitor General observes, a major purpose of section 11501 was to allow federal court scrutiny of these and similar outmoded procedures that systematically inflated rail transportation property valuations and resulted in discriminatory taxation, and it would make little sense to say that courts are powerless to redress "the cause of the problem Congress sought to remedy." U.S. Br. 16-17; see also Petr. Br. 36-37. Yet here too, under respondents' rule, the district court would have to accept replacement cost value as "the true market value" even if the court concluded that this method were biased and yielded falsely inflated values.

Respondents' proposed standard is not simply atextual; it is unfaithful to the clear intent expressed in the text. And to so hold, this Court need not decide whether either the stock-and-debt approach or the replacement cost approach is deficient. Rather, this Court need only decide that railroads should *not* be categorically precluded from arguing, and federal courts should *not* be categorically precluded from finding, that those methods do not yield the best evidence of value in any particular case.

The 4-R Act is a sweeping antidiscrimination statute enacted to cure years of systematic, financially damaging state tax discrimination against railroads, which was often accomplished by use of discriminatory valuation methodologies. Petr. Br. 35-39; U.S. Br. 9, 16-17; S. Rep. No. 87-445, at 451 ("outdated procedures" for assessing property "are sometimes

deliberately retained"). Under respondents' test, a state authority would be free to employ discriminatory methods that inflate the valuation of a particular railroad in a given year, so long as the method was not unreasonable in some undefined sense. Indeed, insulating the selection of methodology from judicial scrutiny merely invites state appraisers to practice discrimination by that means. Petr. Br. 36-37; AAR Br. 15. Congress did not enact a self-defeating statute. The experiences of CSXT and other railroads in Georgia are a mere foretaste of the gaping enforcement loophole that adoption of either the Eleventh Circuit's, or respondents', rule would open. Petr. Br. 37-38 & n.12; AAR Br. 19 & n.13.

3. Congress could have chosen to create a federal administrative review remedy in which deference was paid to the state authorities' valuation decisions, but it logically chose not to do so, U.S. Br. 10, because requiring deference to the state appraisers' valuation methods would have neutered the statute, AAR Br. 14-16; Petr. Br. 30-33. Instead, subsection (b)(1) clearly mandates that the district court make an independent determination of the fact of "the true market value of the rail transportation property." Thus, in a subsection (b)(1) case, the district court's finding of discrimination does not turn upon whether the State's methodology is unreasonable, arbitrary, or animated by discriminatory purpose. Moreover, the district court does not examine whether States use the same or different valuation methods for railroad and commercial and industrial property. And even if the district court finds a violation, it does not enjoin the State from using any particular valuation method or technique in future valuations and assessments. Instead, subsection (b)(1) creates a *de novo* federal remedy whereby discrimination is proven according to a statutory formula. It is an outcome-based discrimination test that depends upon a comparison between the assessed-to-market value ratios for rail transportation property and other commercial and industrial property. AAR Br. 21. If the rail transportation property ratio is more than 5% higher than the counterpart for other commercial and industrial property, the

court may order injunctive relief, but "only to the extent of any portion based on excessive values." Pub. L. No. 94-210, § 306, 90 Stat. 31, 54 (1976).

"[*T*]*he true* market value of the rail transportation property" is one of the critical questions of fact that the district court must determine in applying the federal standard. Under a natural reading of the statute, railroads should be able to put on evidence regarding the true market value of its rail transportation property, using any valuation methodology supported by reliable expert testimony. There is nothing in subsection (b)(1) that justifies the arbitrary exclusionary rule crafted by the Eleventh Circuit (which respondents do not defend), nor the modified version of it advanced by respondents. Congress did not make "true market value" an element of a (b)(1) discrimination claim, and then deprive the railroads of their ability to prove it.

4. Even aside from the impermissibility of adding words to the statute, respondents' construction is based on the false premise that "the true market value" of a property is derived by plugging data into a particular methodology. Resp. Br. 8, 18. That is not how professional appraisers (including state tax appraisers) actually value property; it is not even how Georgia's own appraiser proceeded in this case.

Professional appraisers do not find the "value" of property by recourse to a single valuation methodology. Different methods provide different "evidences" of market value, and appraisers routinely use several different methods to help ascertain the "true market value" of a property. Petr. Br. 6-12; U.S. Br. 9-10, 19-22, 24-26. The selection of valuation methodologies for any particular property requires an appraiser to exercise professional judgment based on factors like the characteristics of the property being valued and the available data. See Petr. Br. 11-12 (citing appraisal treatises); U.S. Br. 19-21; AAR Br. 18-19. The idea that the number produced by one preselected methodology will equal "value" is entirely foreign to the discipline of property appraisal, which recognizes that

value is not the product of formulas and instead is a matter of expert opinion and judgment.

Respondents sidestep these principles, but do not (and cannot) question them. Nor do they question that Congress was well aware of how property appraisals are conducted, and enacted section 11501 against this background understanding. See Petr. Br. 26. As *amicus curiae* the Association of American Railroads ("AAR") notes, the cases cited in the legislative history of section 11501 reveal that Congress recognized that an assessment of the parties' competing valuation methodologies was a necessary step in determining market value. See AAR Br. 23 n.17.

Because property appraisers normally utilize several different methodologies, each of which produces "evidence of value" that may be considered in an expert's formulation of an opinion of value, the claims of respondents and the Eleventh Circuit that the state appraiser's choice of particular valuation techniques are matters of sovereign state "policy" are contrived. Whether a stock-and-debt approach or an income approach (and if the latter, whether a discounted cash flow or a yield capitalization technique) yields better evidence of CSXT's unit value are questions of fact to be decided based on CSXT-specific data and professional judgment, not matters of state policy. *Suitum* v. *Tahoe Reg'l Planning Agency*, 520 U.S. 725, 741-42 (1997) (even in the absence of a functioning market, the market value of property is "simply an issue of fact about possible market prices," and in such cases, the courts typically determine value and valuation methods on the basis of "'opinion evidence'").

Respondents gain no ground by pointing out that "the true market value of rail transportation property" cannot be exactly determined (since there is no functioning market for sales of such property). Resp. Br. 19. That does not make this element of a (b)(1) claim a "'fiction,'" as respondents maintain. *Id.* Even if not empirically observable, the true market value of a property is still a question of fact commit-

ted to the judgment of the district court, as are many kinds of facts that require estimation, economic or scientific modeling, and expert testimony. In many contexts, courts routinely treat not only the ultimate question of market value but also the selection of a valuation methodology as a question of fact to be determined by the factfinder. See Petr. Br. 27-30 (detailing other contexts where choice of valuation methodology is treated as a factual question). No party (even a state party) is entitled to deference on what evidence a district court may rely upon in finding a fact necessary to adjudicate a (b)(1) claim.

Indeed, the district court itself recognized that in "a more typical case" it would consider both sides' expert evidence regarding appropriate methodologies, approaches, and techniques to determine true market value. JA 207 n.8.[2] There is no reason for (b)(1) cases to be treated as atypical cases in which one side's factual assertions about appropriate valuation methods are entitled to an irrebuttable presumption of correctness.

5. Finally, aside from its irreconcilability with the plain language and purpose of the statute, the rule of deference that respondents advocate is indeterminate. *Supra*, at 7-8; Petr. Br. 40. As the Solicitor General points out, "[i]n most instances, there will be no single state 'methodology' to which the court could defer." U.S. Br. 19. That is because, as noted above, state appraisers, following professional practice, will generally use multiple methods to generate evidence of value and then derive a point estimate of value. That final valuation may differ from any of the calculated values. Appraisal Inst., *supra*, at 600. That is what Georgia's appraiser did here; he

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[2] Thus, contrary to respondents' assertions that the district court carefully analyzed and considered the competing expert testimony at trial, *see* Resp. Br. 6 n.6, 34 n.16, the district court clearly explained that it could not and did not consider the unquestionably well-qualified opinion of value—the ultimate issue in the case—offered by CSXT's appraisal expert. JA 207 n.8.

used three different valuation methods to calculate value, and then chose a value that (while close to the value calculated under a yield capitalization approach) corresponded to none of the calculated values. Petr. Br. 14-15. State appraisers do not arrive at a market value of rail transportation property by "correctly applying" a single preselected methodology, and Congress did not impose such a counterproductive rule on district courts. Respondents' rule of deference to a state appraiser's "choice" of a particular analytical technique thus has no foundation in the statute or in valuation practice.

This Court should adhere to the plain meaning of subsection (b)(1). As this Court has declared, the "reach" of subsection (b)(1) and its companion provisions is "straightforward": "Congress prohibited discriminatory tax rates and assessment ratios *in no uncertain terms*, and set forth *precise standards for judicial scrutiny of challenged rate and assessment practices*." *ACF*, 510 U.S. at 337, 343 (internal citation omitted) (emphasis added). The "precise standard" of subsection (b)(1) requires a comparison of the assessed-to-true market value ratios of railroad transportation and other commercial and industrial property, and "[i]t is clear from this language that in order to compare the actual assessment ratios, it is necessary [for a district court] to determine what the 'true market values' are." *Okla. Tax*, 481 U.S. at 461. The statute vests the district court with the power to determine the fact question of "true market value" of property without qualification. Nothing in the statute limits the district court to applying state methodologies or restricts the evidence of market value the district court may consider in resolving that question of fact. This Court should not write into the statute the exclusionary rule respondents favor.

6. Surrounding provisions of the statute reaffirm the plain meaning of § 11501(b)(1). Petr. Br. 33-34. *First*, subsection (c) states that "[t]he burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. § 11501(c). This provision demonstrates that Con-

gress intended an evidentiary hearing on true market value, and that it knew how to impose procedural restrictions when that was its intent. Petr. Br. 33-34; U.S. Br. 13-14; AAR Br. 24. Noticeably *absent* from this provision is *any* restriction on what valuation evidence courts may consider in determining "true market value."

Second, subsection (c)'s provisions regarding proof of the market values of other commercial and industrial property in the assessment jurisdiction at issue underscore that the district court independently determines the true market value of all property, including rail transportation property, regardless of what methods the state appraiser employs. This provision requires that a specific statistical sampling method (the "sales assessment ratio study") be used in determining the ratio of assessed to true market value for the other commercial and industrial property in the relevant assessment jurisdiction. Petr. Br. 34-35. The ratio must be proved "*to the satisfaction of the district court*," and if this cannot be done, alternative methods are provided. 49 U.S.C. § 11501(c) (emphasis added).

Respondents draw the wrong conclusion from subsection (c). They focus on the nature of the presumptive statutory method for valuing commercial and industrial property, and make the illogical leap of reasoning that because railroad value cannot be likewise estimated from actual sales data, Congress must have intended deference to the State defendants' choice of valuation techniques. The more natural inference is that since Congress did not require district courts to defer to any state method for valuing commercial and industrial property, it likewise did not require courts to defer to any state methods for valuing rail transportation property. Moreover, respondents wholly ignore subsection (c)'s requirement that the ratio of assessed value to "true market value" of other commercial and industrial property must be proven "to the satisfaction of the district court." Because "identical words and phrases within the same statute should normally be given

the same meaning," *Powerex Corp.* v. *Reliant Energy Servs., Inc.*, 127 S. Ct. 2411, 2417 (2007), Congress's use of the identical term—"true market value"—with respect to rail transportation property must likewise refer to the value of the property as determined by the court without deference to the State's preferred method. See Petr. Br. 33-35; U.S. Br. 14-16.

7. Respondents' invocation of federalism principles is unavailing. Respondents devote little space to the policy of the 4-R Act but much to the Tax Injunction Act, 28 U.S.C. § 1341, and decisions refusing to construe federal statutes, such as 42 U.S.C. § 1983, as authorizing injunctive relief against state tax practices (*e.g.*, *Nat'l Private Truck Council, Inc.* v. *Okla. Tax Comm'n*, 515 U.S. 582 (1995)). But as respondents concede, Resp. Br. 10, in the 4-R Act Congress "declared an exception from the provisions of the Tax Injunction Act, 28 U.S.C. § 1341, allowing railroads to challenge discriminatory taxation in federal district courts." *Okla. Tax*, 481 U.S. at 457-58; 49 U.S.C. § 11501(c) ("Notwithstanding section 1341 of title 28 . . . , a district court of the United States has jurisdiction . . . to prevent a violation of subsection (b) of this section."). The presumption against interference with state tax collection is thus overcome; Congress found the creation of such a federal remedy to be necessary given the enduring practices of discrimination. The only issue is whether, having defined "precise standards for judicial scrutiny of challenged rate and assessment practices," *ACF*, 510 U.S. at 343, Congress intended to restrict the evidence that the district court could consider in adjudicating the fact question of "the true market value of rail transportation property." For all the reasons given above, the answer is plainly no.

Respondents fare no better in invoking the *Gregory* clear statement canon. As noted above, that canon applies only when the statutory provision is "susceptible of two plausible interpretations, one of which would have altered the existing balance of federal and state powers." *Salinas*, 522 U.S. at 59-60. Respondents' construction is not a "plausible interpreta-

tion" of subsection (b)(1), and allowing a district court to consider expert testimony on market value using different valuation techniques than the State's appraiser employed would not alter the federal-state balance. See Petr. Br. 41-42.

Indeed, respondents themselves do not take seriously the clear statement canon they urge upon the Court. Their eleventh-hour interpretation that a court may determine whether the State's valuation method is "reasonable" has no textual support whatsoever, for nowhere does the 4-R Act expressly allow the federal court to evaluate the reasonableness of the State's chosen methodology. While respondents' interpretation is incorrect and unworkable, the fact that respondents proposed it fatally undermines their contention that *Gregory* has any application here.

Finally, respondents rely on *ACF*, Resp. Br. 12-13, but never address CSXT's showing that (1) in *ACF*, unlike this case, this Court found that the taxpayers' construction of the subsection at issue (subsection (b)(4)) was contrary to its plain meaning, when interpreted in light of surrounding provisions; (2) the federalism canon invoked was the rule (inapposite here) against inferring preemption beyond the "evident scope" of a narrow provision, 510 U.S. at 345; and (3) the position advocated by the taxpayers there actually encroached upon state sovereignty, jeopardizing a State's critical legislative power to grant exemptions from state *ad valorem* taxation. See Petr. Br. 45-47; see also U.S. Br. 29-30; AAR Br. 19 n.12. *ACF* provides respondents no support in this case.

8. Like their appeal to federalism canons, respondents' comity-based arguments have no force. In *Oklahoma Tax*, this Court summarily dismissed similar arguments based on "principles of comity" that relied on the supposed burden of federal court valuation proceedings and the interference with state tax collection efforts. This Court declared that "[t]hese are policy considerations which may have weighed heavily with legislators who considered the Act and its predecessors.

It should go without saying that we are not free to reconsider them now." 481 U.S. at 464.

In any event, respondents' policy arguments are overstated. Respondents complain that CSXT's interpretation "would turn the district courts into federal boards of equalization required to oversee protracted, complicated battles between expert witnesses over whose method is 'best.'" Resp. Br. 23. But contested valuations of property are commonplace in the federal courts. Petr. Br. 27-30. Moreover, although valuation cases since *Oklahoma Tax* have been too infrequent to pose any threat of undue burden on the federal courts, see AAR Br. 13 & n.9, respondents concede that after *Oklahoma Tax* extensive trials will be conducted (at a minimum) on the application of valuation methodologies. Resp. Br. 7, 33-34. Allowing the district court to hear a case under subsection (b)(1) as "a more typical [valuation] case," JA 207 n.8, and to consider expert testimony on which valuation techniques provide the best evidence of true market value, do not appreciably affect the complexity or burden of 4-R Act proceedings.[3]

In addition, the marginal effect on state tax administration practices is minimal. Respondents do not dispute that 4-R Act injunctions only prevent the collection of excessive tax in the year in question; courts do not enjoin States from using any valuation methods. U.S. Br. 10, 17; AAR Br. 21; Petr. Br. 49-50. Respondents nonetheless claim that States "will have no real choice but to change [their] assessment practices" if their interpretation is not adopted. Resp. Br. 32. That argument is unsound for a number of reasons. First, it is predicated on the incorrect supposition that state appraisers typically use one appraisal method to determine true market value, which must be changed if the railroad prevails in a

[3] As Congress heard in hearings before enacting section 11501, techniques to value railroads were "neither incomprehensible nor overly complicated," and in fact had reached "a substantial degree of refinement." *Tax Assessments on Common Carrier Property: Hearing on H.R. 736 and H.R. 10169 Before the Subcomm. on Transp. and Aeronautics of the H. Comm. on Interstate and Foreign Commerce*, 88th Cong. 18 (1964).

(b)(1) challenge. See Petr. Br. 8-12. Indeed, this case proves that States do not use just one appraisal method—either year-to-year or even in the same year. Petr. Br. 14, 44-45; U.S. Br. 21-22; AAR Br. 19 & n.13.

Second, even if a court decides to put substantial weight on a particular method in determining market value in a given year, that is no reason to assume that courts will do the same in following years; a court adjudicating a subsection (b)(1) claim for a specific tax year simply makes a determination, based on the available data, that such a method yielded the best evidence of the true market value of a railroad's transportation property in that year.

Third, both the underlying railroad data and the data for other commercial and industrial property shift every year, so a valuation technique that results in injunctive relief in one tax year may not in the next, if the railroad ratio in the next year is no longer 5% higher than the ratio for other commercial and industrial property. See 49 U.S.C. § 11501(c).

Fourth, to the extent States are choosing valuation methods that discriminate against railroads systematically, thus flouting the Act's terms, there is nothing to lament if as a practical matter the States are forced to abandon such practices. See S. Rep. No. 87-445, at 448 (state tax discrimination against railroads "results" in large measure from "outmoded assessing procedures" employed at the state level); *id.* at 451 ("outdated procedures" for assessing property "are sometimes deliberately retained").

Finally, respondents' position trivializes federalism. Federalism is about respect for and noninterference with matters important to state sovereignty, such as final criminal judgments, ongoing state judicial and administrative proceedings, and state administration of prisons and schools. It would be beyond odd to include in that company the selection of valuation methodologies, particularly when States delegate the power to select methodologies to state appraisers who can and do change the methods from year to year. See *supra*, at 7-8,

14-15; Petr. Br. 14-15, 37 & n.12. The fact that not a single state Attorney General filed an *amicus* brief in support of respondents attests to the absolute absence of a core federalism interest in this case.

9. When Congress has spoken plainly to the matter at hand, as it has done with § 11501(b)(1), the Court's inquiry comes to an end and resort to legislative history is unnecessary. *Okla. Tax*, 481 U.S. at 461 (rejecting similar arguments of the state respondents from legislative history). However, should this Court choose to consider the 4-R Act's legislative history, that history supports the plain text.

Respondents attempt to turn to their advantage certain statements of witnesses representing various railroads or the AAR in congressional hearings that purportedly expressed lack of concern about railroad valuation methods used by the States. Resp. Br. 29-31. As an initial matter, comments of individuals at committee hearings are entitled to *no* weight because this Court "decline[s] to accord any significance to . . . statements" that were *not* "made by a Member of a Congress, nor . . . included in the official Senate and House Reports." *Kelly* v. *Robinson*, 479 U.S. 36, 51 n.13 (1986); see also *McCaughn* v. *Hershey Chocolate Co.*, 283 U.S. 488, 493-94 (1931) ("statements . . . made to committees of Congress . . . are without weight in the interpretation of a statute"); 2A Norman J. Singer, *Sutherland Statutes and Statutory Construction* § 48:10 (7th ed. 2007). Respondents' contention that a court should give weight to the views of private witnesses representing industry—"because the railroad *industry* was in effect the primary sponsor of the legislation," Resp. Br. 31 (emphasis added)—is unknown to this Court's precedents. Such a novel canon should be summarily rejected, as it would allow courts to stray from *Congress's* plainly expressed intent.

Moreover, clutching at isolated statements of hearing witnesses betrays the weakness of respondents' analysis of the legislative history. Regardless of the importance that these

particular industry witnesses attached to state valuations,[4] it is uncontroverted that Congress's vexation with the States' use of unfair and discriminatory valuation practices was one of the driving forces behind the Act. Respondents even *concede* that Congress acted out of "real concern" regarding the States' discriminatory use of "'outmoded' or 'outdated' procedures" in valuing railroad properties. Resp. Br. 35 (quoting S. Rep. No. 87-445, at 448); see Petr. Br. 36 (same). Respondents attempt to cover this flank by claiming that Congress intended district courts to distinguish binding state methods from unreasonable state methods, Resp. Br. 35, even though

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[4] Respondents overread the witness statements upon which they rely. James Ogden testified on behalf of the AAR that the "principal problem" was discriminatory assessment rules for different kinds of property rather than the inadequacy of railroad valuation methods. *Tax Assessments on Common Carrier Property: Hearing on H.R. 736 and H.R. 10169 Before the Subcomm. on Transp. and Aeronautics of the H. Comm. on Interstate and Foreign Commerce*, 88th Cong. at 18-19. While that was a major problem corrected by the 4-R Act, *see* Petr. Br. 45, nothing in Ogden's statement suggests that discrimination caused by the State's choice of improper valuation methods was not also a problem, or that district courts were not free to reject such methods in resolving the fact question of the true market value of rail transportation property. Similarly, Philip Lanier's reference to "the valuation question" not being "our problem," *State Tax Discrimination Against Interstate Carrier Property: Hearing on S. 2289 Before the Subcomm. on Surface Transp. of the S. Comm. on Commerce*, 91st Cong. 39 (1969) ("*Hearing on S. 2289*") (statement of Philip M. Lanier, Vice President, Louisville & Nashville Railroad), meant only that he did not intend for Congress to dictate to the States which methods they should use. *See Common and Contract Carrier State Property Tax Discrimination: Hearing on H.R. 16245 Before the Subcomm. on Transp. and Aeronautics of the H. Comm. on Interstate and Foreign Commerce*, 91st Cong. 138 (1970) (statement of Philip M. Lanier, Vice President, Louisville & Nashville Railroad) (the legislation "would not deal with valuation being standard"). Indeed, Lanier was a proponent of an independent judicial determination of true market value. *See Hearing on S. 2289*, 91st Cong. at 40 (statement of Philip M. Lanier, Vice President, Louisville & Nashville Railroad) ("a multifactor formula is better for railroads because at best it is a matter of judgment as to the value, and there are several good indicators of value").

Congress said nothing of the sort in the statute or otherwise. And it is not surprising that Congress was silent, since respondents' rule is judicially unadministrable—requiring courts to enter the unknown thicket of distinguishing valuation methods that are not "reasonable" from those that, while reasonable in some undefined sense, are not the most appropriate methods under the circumstances. Thus, the far simpler solution is to give subsection (b)(1) its plain meaning, and permit district courts applying the (b)(1) discrimination test to make a fully independent determination of market value without having to adhere slavishly to the valuation methods endorsed by the State's appraiser.[5]

10. Respondents devote the final section of their brief to arguing an issue not presented: whether subsection (b)(1) would permit a district court to value rail transportation property according to the unit-value method when state law requires the inventory method. Respondents attempt this shift in focus because a state choice of a unit-value versus an inventory method arguably implicates state policy—unlike a state appraiser's choice between different income techniques for estimating the unit value of a particular railroad, which is the question presented here. If this Court wishes to reach that question, the answer is that there is no state policy exception to the 4-R Act.

Subsection (b)(1) defines a precise federal formula for determining discrimination based on comparing the ratios of assessed-to-market value of rail transportation property and other commercial and industrial property. Unit valuation is

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[5] Respondents also claim that their rule of deference captures the "latitude" that purportedly this Court gave States in resolving constitutional challenges to railroad valuations prior to passage of the 4-R Act. Resp. Br. 36-40; *see also Amicus Curiae* Multistate Tax Commission ("MTC") Br. 10-12 (citing cases involving constitutional challenges). This argument lacks force. The fact that this Court gave States "latitude" to overvalue rail transportation property in deciding *constitutional* challenges is irrelevant to the standards that Congress intended be set in a § 11501(b)(1) proceeding.

universally regarded as the most reasonable means of valuing rail transportation property. Petr. Br. 8. If an outlier State like Virginia were to assess rail transportation property at a higher ratio to its true market value than other commercial and industrial property by employing an inventory method to value rail transportation property, subsection (b)(1) provides the railroad a remedy. Congress's concern was remedying discrimination. In deciding whether the State defendants have discriminated, the district court makes an independent determination of the fact of "true market value." Where a federal violation is proven, the railroad is entitled to relief no matter what valuation methods States employ. Indeed, the courts have found 4-R Act violations when practices were sanctioned by state statutes and even state constitutions. Petr. Br. 39, 45.[6] The Supremacy Clause requires no less.

* * * *

Redressing decades of state and local tax discrimination, Congress provided railroads a federal court remedy "in no uncertain terms," *ACF*, 510 U.S. at 343, and vested district courts with the power to determine "the true market value of rail transportation property" in applying the statutory federal discrimination standard. Congress did not abridge or qualify that power in any dimension, and this Court should not craft an unfounded exclusionary rule that would shelter the very discrimination Congress intended to forbid.

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[6] *Amicus curiae* MTC claims that a handful of States have codified a methodology policy choice in their statutes, *see* MTC Br. 8, but all of the statutes it cites require or permit consideration of multiple methodologies, as well as leave discretion to the state appraisers to decide what weight to give the various methodologies in determining true market value. Ala. Code § 40-21-6; Ark. Code Ann. § 26-26-1607; Colo. Rev. Stat. § 39-4-102; Fla. Stat. § 193.011. Regardless, even if any State were in the future to legislate a single valuation methodology for an appraiser to apply, that would not overcome the plain meaning of the 4-R Act.

CONCLUSION

For the foregoing reasons and those stated in CSX's opening brief, the judgment should be reversed and the case remanded for a new trial.[7]

Respectfully submitted,

ELLEN M. FITZSIMMONS
DAVID J. BOWLING
CSX CORPORATION
500 Water Street
Jacksonville, FL 32202
(904) 359-3200

CARTER G. PHILLIPS*
STEPHEN B. KINNAIRD
ILEANA M. CIOBANU
MATTHEW J. WARREN
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000

PETER J. SHUDTZ
CSX CORPORATION
1331 Pennsylvania Ave., NW
Washington, DC 20004
(202) 783-8124

JAMES W. MCBRIDE
BAKER, DONELSON,
BEARMAN, CALDWELL
& BERKOWITZ, PC
555 Eleventh Street, NW
6th Floor
Washington, DC 20004
(202) 508-3400

Counsel for Petitioner

October 22, 2007

* Counsel of Record

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[7] Respondents wrongly claim that on remand CSXT is not entitled to a new trial. *See* Resp. Br. 43. Because the district court's determination that it was barred from considering CSXT's evidence is the functional equivalent of excluding evidence, JA 214-16, and because under the court of appeals' ruling, "[t]he district court was not allowed to consider a valuation methodology different from the methodology of the Board," Pet. App. 15a, on remand the district court must consider the proper weight to give CSXT's expert evidence on true market value in a new trial.

(4)

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In the Supreme Court of the United States

CSX TRANSPORTATION, INC., PETITIONER

v.

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ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONER

PAUL D. CLEMENT
Solicitor General
Counsel of Record
PETER D. KEISLER
Assistant Attorney General
THOMAS G. HUNGAR
Deputy Solicitor General
DOUGLAS HALLWARD-DRIEMEIER
Assistant to the Solicitor General
ANTHONY J. STEINMEYER
ROBERT D. KAMENSHINE
Attorneys
Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

D.J. GRIBBIN
General Counsel
Department of Transportation
Washington, D.C. 20590

ELLEN D. HANSON
General Counsel
Surface Transportation Board
Washington, D.C. 20423

QUESTION PRESENTED

Whether, in an action by a railroad under 49 U.S.C. 11501(b)(1) claiming that a State has assessed the railroad's property at a higher ratio of assessed value to true market value than the ratio for other commercial and industrial properties, the district court may, in determining the railroad's true market value, consider evidence of market value derived from accounting methodologies other than those used by the State, or whether, as the court of appeals held, the State's chosen methodology is binding on the district court.

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In the Supreme Court of the United States

No. 06-1248

CSX TRANSPORTATION, INC., PETITIONER

v.

GEORGIA STATE BOARD OF EQUALIZATION, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONER

INTEREST OF THE UNITED STATES

This case concerns the scope of federal protection against discriminatory state taxation provided to railroads by Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 (4R Act), Pub. L. No. 94-210, 90 Stat. 54 (49 U.S.C. 11501). The Surface Transportation Board—the independent federal agency with responsibility for the economic regulation of the Nation's railroads, 49 U.S.C. 721—is charged with fostering economic conditions that allow rail carriers to earn adequate revenues. The Department of Transportation is the federal agency charged with, among other functions, overseeing rail safety, 49 U.S.C. 20103 (2000 & Supp. IV 2004), and thus also has an interest in the financial health of the Nation's railroads. The United States has participated as amicus curiae in previous cases regarding the scope of the 4R Act's protections. See *Burlington N. R.R.* v. *Oklahoma Tax*

Comm'n, 481 U.S. 454 (1987) (*Burlington Northern*); *Department of Revenue* v. *ACF Indus., Inc.*, 510 U.S. 332 (1994) (*ACF*).

STATEMENT

1. The 4R Act was enacted in response to the economic deterioration of the rail industry. See 4R Act § 101, 90 Stat. 33. Section 11501, originally Section 306 of the 4R Act, focuses on discriminatory state taxation as a particular cause of that decline. See § 306, 90 Stat. 54 (49 U.S.C. 11501); H.R. Rep. No. 725, 94th Cong., 1st Sess. 78 (1975).[1] After 15 years of study, Congress had found that discriminatory state taxation of railroad property "constitute[s] an unreasonable and unjust discrimination against, and an undue burden on, interstate commerce." 4R Act § 306, 90 Stat. 54 (49 U.S.C. 26c(1) (1976)). In order to protect those critically important channels of interstate commerce, Congress took the extraordinary step of carving out an exception to the Tax Injunction Act, 28 U.S.C. 1341, and empowered federal courts to enjoin prohibited forms of discriminatory state taxation. 4R Act § 306, 90 Stat. 54 (49 U.S.C. 11501(c)).

Section 11501 specifies certain forms of prohibited discrimination and also broadly prohibits States from imposing any other "tax that discriminates against a rail carrier providing transportation." 49 U.S.C. 11501(b)(4). With respect to tax assessments (and taxes levied or collected on the basis of such assessments) in particular, the statute requires that a State's

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[1] The statutory language of the original 4R Act was altered slightly when Section 306, originally codified at 49 U.S.C. 26c (1976), was recodified in 1978 at 49 U.S.C. 11503 (1994) as part of the positive enactment of Title 49. See Act of Oct. 17, 1978 (1978 Act), Pub. L. No. 95-473, 92 Stat. 1337. The restatement of prior law effected by the 1978 reenactment was "without substantive change." 1978 Act § 3(a), 92 Stat. 1466. In 1995, the provisions of Section 11503 were again reenacted without substantive change but renumbered as Section 11501, as part of a general amendment of Subtitle IV of Title 49 that abolished the Interstate Commerce Commission and created the Surface Transportation Board. ICC Termination Act, Pub. L. 104-88, § 102(a), 109 Stat. 804.

(or political subdivision's) assessment of railroad property for purposes of an ad valorem tax be tested by a simple comparison of two arithmetic ratios. Under that test, a State's assessment practices are unlawfully discriminatory if the ratio of assessed value to "true market value" (assessment ratio) for railroad property exceeds the assessment ratio for "all other commercial and industrial property." 49 U.S.C. 11501(b)(1).

The statute expresses a preference for establishing the assessment ratio for non-railroad commercial and industrial property "through the random-sampling method known as a sales assessment ratio study." 49 U.S.C. 11501(b)(1).[2] If the assessment ratio for non-railroad commercial and industrial property cannot be established satisfactorily by that method, the statute then requires the court to enjoin any discrimination that is revealed by a comparison of the railroad's assessment ratio to the assessment ratio for "*all other property* subject to a property tax levy in the assessment jurisdiction," *i.e.*, a ratio not limited to commercial and industrial property. 49 U.S.C. 11501(c)(1) (emphasis added).[3]

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[2] A "sales assessment ratio study" compares the assessed value to the actual sale price for a representative and statistically valid sample of property within the assessment jurisdiction. See International Ass'n of Assessing Officers, *Improving Real Property Assessment: A Reference Manual* 122-155 (1978).

[3] Section 11501(c)(1) contains a scrivener's error, which was introduced when Title 49 was recodified and enacted as positive law in 1978. In the original 4R Act, Congress provided unambiguously that the alternative comparison ratio (if a sales assessment ratio study of commercial and industrial property was inadequate) was the ratio of assessed value to true market value of "all other property in the assessment jurisdiction" subject to tax, *i.e.*, not just the ratio of assessed to market value of other commercial property. See 4R Act § 306, 90 Stat. 55 (49 U.S.C. 26c(2)(e) (1976)). In 1978, when Congress recodified Title 49, the words "commercial and industrial" were inserted into the description of the denominator of that alternative ratio, but no similar limitation was added to the numerator, which continues to refer to "all other property subject to a property tax." 1978 Act § 11503(c)(1), 92 Stat. 1446 (49 U.S.C. 11501(c)(1)). The House Report made no reference to the change. See H.R. Rep. No. 1395, 95th Cong., 2d Sess. 179 (1978). Comparison of the railroad's assessment ratio to the ratio indicated by the literal terms of the

A federal court that finds state property tax assessments to discriminate against railroads is empowered to enjoin the violation. 49 U.S.C. 11501(c). Congress limited the impact of the anti-discrimination prohibition, however, by barring the district court from granting any relief under Section 11501 unless the assessment ratio for the railroad's property exceeds the assessment ratio for other commercial and industrial property by at least 5%. *Ibid.*

2. In Georgia, public utilities (*i.e.*, railroads, investor-owned electric utilities, investor-owned telephone companies, pipeline companies, and gas distribution companies) are assessed at the State level. The State Revenue Commissioner, acting on proposed assessments prepared by the Property Tax Division of the Georgia Department of Revenue (Department), certifies the proposed assessments to each county in which there is taxable property. Pet. App. 2a-3a. Other properties, including non-utility commercial and industrial properties, are assessed locally. See *id.* at 2a.

Georgia, like most States, assesses public utilities using the "unit rule," under which the appraiser "values the entire operating system * * * as a going concern and integrated whole irregardless of where it is located," Pet. App. 30a, and then multiplies the value of the whole unit "by the percentage of the entity located within Georgia to determine what portion of the company should be allocated to the state," *id.* at 3a.

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statute would be nonsensical, because the latter ratio would be a meaningless apples-to-oranges comparison of vastly disparate classes of property. Because the statute would be absurd if applied as written, and because Congress specified that the enactment of Title 49 was a restatement of prior law "without substantive change," that could "not be construed as making a substantive change in the laws replaced," § 3(a), 92 Stat. 1466, the reenactment's introduction of the words "commercial and industrial" in the denominator of the comparison ratio in Section 11501(c)(1) must be deemed a scrivener's error. Although this Court quoted the "commercial and industrial" language from Section 11501(c)(1) in *Burlington Northern*, 481 U.S. at 462, that language was not itself at issue and the Court did not analyze the significance of the statutory change.

The alternative "summation" method, employed by some States, is to calculate the value of each individual item of taxable property owned by the taxpayer within the State in isolation and to then aggregate those discrete values. See Committee on Unit Valuation, National Association of Tax Adm'rs, *Appraisal of Railroad and Other Public Utility Property for Ad Valorum Tax Purposes* 2 (1954) (Unit Valuation Report).

The methods used to value a company under the unit rule "fall into three general categories: the sales comparison approach, the cost approach, and the income approach," Pet. App. 3a, which, as their names suggest, derive estimates of value from, respectively, "actual sales of comparable companies or properties," the cost of the company's property, or the company's predicted future income stream. *Ibid.* There are variations within each of those three basic approaches as well. For example, under the cost approach, one could select between original cost or reproduction cost. See Unit Valuation Report 7-8.

In *Burlington Northern*, this Court held that the district court could review a railroad's claim that the State had violated the 4R Act's prohibition against discriminatory assessment ratios by overvaluing the railroad's assets. The Court rejected the State's position that the federal courts must accept "whatever the State determines the value of the railroad to be." 481 U.S. at 461-462. Further, the Court held that a railroad need not show that "the overvaluation results from discriminatory intent." *Id.* at 463.

In so holding, the Court noted that the railroad's "sole challenge [was] to the application of [the State's] methodology." *Burlington Northern*, 481 U.S. at 463 n.5. Thus, the Court expressed "no view" as to "whether a railroad may * * * challenge * * * the appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual deter-

minations to which the State's preferred accounting methods were applied." *Ibid.*

3. Petitioner, a freight rail carrier that has multiple routes through Georgia, brought this action under Section 11501 in the United States District Court for the Northern District of Georgia against Georgia's State Board of Equalization to challenge the proposed valuation of the railroad's operating property for ad valorem tax purposes. Pet. App. 24a-25a. Petitioner claimed that for the tax year 2002 the Georgia tax authorities had overestimated the true market value of its transportation property by valuing it at $7.8 billion when its "true market value * * * did not exceed $6 billion." *Id.* at 7a. As a result, the assessment ratio for its property—when the correct market value was used—exceeded the ratio for non-railroad commercial and industrial property within Georgia.

In 2002, the Department's appraiser, Gregg Dickerson, made certain changes to the manner in which the State calculated value under the unit rule. Pet. App. 4a. He discarded a "capitalized earnings approach" and a "direct capitalization approach," two income approaches, in favor of another income approach—the discounted cash flow approach (DCF)—and a "market multiple approach," which values the company by multiplying its income by a multiple derived from the ratio of stock price to income for companies engaged in similar lines of business. Pet. App. 35a. Dickerson retained a "stock and debt approach," which the State had already been using. *Ibid.* For the market multiples approach, Dickerson utilized three different multiples. *Id.* at 5a. He thus derived "five values from these three methods" which ranged from $8.126 billion to $12.346 billion. *Ibid.* "As he did with all public utilities that year, Dickerson selected an amount at the lower end of that range," $8.2 billion, in an effort "to avoid potential litigation." *Ibid.* He then deducted $400 million "to account for intangible property not subject to *ad valorem* taxation" in Georgia, yielding a final taxable valuation of $7.8 billion. *Ibid.*

In support of its claim, petitioner offered a valuation report prepared by its own appraiser, Thomas Tegarden, whose credentials the district court deemed to be "impeccable." Pet. App. 25a. Tegarden used three valuation methods, "(1) a stock and debt approach, (2) a cost approach, and (3) a yield capitalization approach," which is "another variation of the income approach." *Id.* at 35a. He concluded that "the unit value of the Railroad for tax year 2002 did not exceed $6 billion." *Id.* at 7a.

4. After a bench trial, the district court concluded that the State "ha[d] not discriminated against CSXT in violation of 49 U.S.C. § 11501(b)(1)." Pet. App. 71a. The court held that "the 4-R Act does not generally allow a railroad to challenge the state's chosen methodology." *Id.* at 42a. Rather, "[a]s long as the Department's chosen valuation methods are rational and were not chosen for the purpose of discriminating against [the railroad], the court will not second guess the Department's choice of methods." *Ibid.* The court explained that "all five approaches used by CSXT and the Department * * * are widely used to value property" and are "accepted valuation methods." *Id.* at 38a.

The court emphasized that, in its view, "the Department used essentially the same valuation methods for CSXT that it used for other centrally assessed taxpayers." Pet. App. 40a. Given that "at least three different valuation methods" had been used by each side's expert to "arrive[] at different conclusions * * * under each method," *id.* at 41a, it was "clear" to the court "that the determination of the true market value of CSXT * * * is, at best, an educated guess." *Id.* at 42a. Finally, the court held that the Department's chosen valuation methods, all of which "are widely accepted and used by valuation experts," *ibid.*, "are rational" and therefore not subject to challenge. *Id.* at 43a.

5. A divided panel of the court of appeals affirmed. Pet. App. 1a-23a. The court began its analysis by concluding that

the principle "that a statute will not be construed to burden states in the exercise of their traditional powers unless it clearly states its intent to do so," *id.* at 11a, was applicable because, in the court's view, "[t]he selection of a valuation methodology is a part of th[e] fundamental power" of the States to tax, *id.* at 12a. In the court's view, moreover, "[t]he text of the Act does not clearly state that railroads may challenge valuation methodologies." *Id.* at 14a.

"[T]o the extent [legislative history] ha[d] any relevance to [the] inquiry," the court stated that the legislative history "supports the conclusion that railroads may not challenge state valuation methodologies in federal court." Pet. App. 14a (quoting *ACF*, 510 U.S. at 345). The court quoted a Senate report on a precursor of Section 306. That report stated that the bill contemplated no change in "assessment standards, assessment practices, or the assessments themselves," but "merely provides a single standard against which all affected assessments must be measured." *Ibid.* (quoting S. Rep. No. 1483, 90th Cong., 2d Sess. 22 (1968)). Accordingly, the court concluded "that railroads may not challenge state valuation methodologies under subsection (b)(1)." *Ibid.*

Judge Fay dissented, "disagree[ing] with the * * * holding that the 4-R Act bars the Railroad from challenging the valuation methodology chosen by the State." Pet. App. 20a. Noting that "there are many methodologies that can be used in assessing the value of property," *id.* at 21a, he observed that "[s]urely a state could not use one method to assess the market value of railroad property and a different method to assess other commercial and industrial property if such resulted in a gross discrimination toward the railroad," *id.* at 21a-22a. Moreover, he reasoned that "a railroad should be allowed to challenge the method used in an attempt to prove that the result of such a method was not the *true market value* of its property." *Id.* at. 23a.

SUMMARY OF ARGUMENT

Section 306 of the 4R Act is an anti-discrimination provision that prohibits de facto discrimination against railroads in state property taxation. One form of discrimination against which the Act expressly protects is the practice of assessing railroads at a higher ratio to their true market value than is true generally of other commercial properties. In order to determine whether such discrimination has occurred, the federal court must ascertain true market value with respect to both the railroad and other commercial properties. The statute expressly contemplates a hearing on that question: it addresses the burden of proof and it specifically references a presumptively preferred method of valuation for other commercial properties that is to be used if the evidence is "to the satisfaction of the district court." 49 U.S.C. 11501(c). Based on those features of the statute, this Court held in *Burlington Northern* that the true market value of the railroad is a matter to be determined by the federal court. The same reasoning that led the Court to that result also compels the conclusion that consideration of valuation methodologies different from those of the State can be part of that determination.

There is nothing sacrosanct about a State's use of a particular methodology in determining a railroad's "true market value"; if that is, in fact, a step in the State's assessment process. In fact, the legislative history reflects that the States' use of certain "outdated procedures," which yielded inflated market values for railroads, was one of the problems that Congress sought to address. The court of appeals' ruling that state methodologies are beyond challenge defeats that purpose. Moreover, the court of appeals' premise—that a State necessarily chooses a single valuation approach—is itself mistaken. The most appropriate valuation approach may vary from property to property based on individual factual circumstances. Moreover, an appraiser often derives multiple indications of value utilizing various approaches, which must be

weighed in light of the particular facts of the case to arrive at a final value that may not correspond to the value indicated by any single method. In that circumstance, as when a State does not even calculate "true market value" as a step in its assessment process, there is no single State "method" to which to defer.

There is, moreover, no clear line of demarcation between the State's choice of a "method" and its "application." In this case, for example, the seemingly different formulae used by the experts are really different ways of stating the same principle, but with slightly different assumptions about petitioner's future income. The court of appeals' broad rule that even the choice among different assumptions in the course of a valuation constitutes unassailable "methodology" cannot be reconciled with *Burlington Northern* and would render state appraisals susceptible to easily implemented, unredressable manipulation.

Federal courts must determine the true market value of property in many different circumstances, a process that necessarily involves judicial resolution of issues of appraisal methodology. There is nothing problematic about the courts doing so in an action under Section 11501(b)(1) as well. Contrary to the court of appeals' apparent assumption, an action under Section 11501(b)(1) is not an administrative law proceeding for deferential review of a state appraiser's valuation, but rather a de novo action to vindicate a federal right to be free from discriminatory state tax assessments. It would be inappropriate in such an action for the federal court simply to defer to the State's valuation.

ARGUMENT

I. IN DECIDING A CLAIM OF DISCRIMINATORY OVERVALUATION UNDER THE 4R ACT, A FEDERAL COURT IS NOT REQUIRED TO ACCEPT THE STATE'S METHOD OF VALUATION

A. In Providing A Remedy Against De Facto As Well As Intentional Discrimination, Congress Required The Federal Courts To Make Independent Determinations Of True Market Value

Congress enacted Section 306 of the 4R Act to address the problem of "discriminatory state taxation of railroad property." *Burlington Northern*, 481 U.S. at 457. Thus, Congress provided a remedy against any tax that "*results in* discriminatory treatment of a common carrier by railroad." 4R Act § 306, 90 Stat. 54 (emphasis added) (49 U.S.C. 26c(1)(d) (1976)).[4] Significantly, as this Court explained in *Burlington Northern*, Congress forbade "'acts' which 'unreasonably burden and discriminate against interstate commerce'" without reference "to the intent of the actor." 481 U.S. at 463 (quoting 49 U.S.C. 11501(b)).

With respect to discriminatory assessments, Section 11501(b)(1) forbids, and Section 11501(c) authorizes the federal courts to enjoin, States from assessing railroad property "at a value that has a higher ratio to [its] true market value" than the corresponding ratio for "other commercial and industrial property." 49 U.S.C. 11501(b)(1). As the Court recognized in *Burlington Northern*, "[i]t is clear from this language that in order to compare the actual assessment ratios, it is

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[4] The 1978 Act replaced the words "results in discriminatory treatment" with "discriminates," see 1978 Act § 11503(b)(4), 92 Stat. 1446 (49 U.S.C. 11501(b)(4)), but that "change[] 'may not be construed as making a substantive change in the laws replaced.'" *Burlington Northern*, 481 U.S. at 457 n.1 (quoting 1978 Act § 3(a), 92 Stat. 1466).

necessary to determine what the 'true market values' are." 481 U.S. at 461. The Court rejected the argument that the federal courts must accept "whatever the State determines the value of the railroad to be." *Id.* at 461-462. The statutory reference to "true market value" is not a reference to a State's definition of value for its own assessment purposes. Rather, the railroad's "true market value" is a federal question "to be litigated in federal court." *Id.* at 462.

In *Burlington Northern*, the railroad had "not challenged the valuation methodology" used by the State to determine the railroad's value, but had limited its challenge to "the application of that methodology." 481 U.S. at 463 n.5. Thus, the Court noted, without deciding, the question "whether a railroad may, in an action under [Section 11501], challenge in the district court the appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied." *Ibid.*

Although *Burlington Northern* reserved the question, its logic requires that the federal court also be able to consider questions of valuation methodology. There is no clear line that separates methodological choices from mere questions of application. Moreover, because, as the district court conceded, it is the State's choice of "a particular methodology that, to a large extent, predetermines the result," Pet. App. 38a, foreclosing any challenge to the State's methodology would essentially eviscerate the protection afforded by Section 11501(b)(1), particularly if "methodology" is understood in the broad sense employed by the courts below.

The *Burlington Northern* Court recognized that Section 11501(b)(1) and (c) plainly require the reviewing court to determine the "true market value" of the railroad's property. There is no indication in the statutory text that Congress intended to bind the federal courts to employ the particular

methodological judgments adopted by state or local government appraisers in performing that inquiry. To the contrary, the statute reflects Congress's understanding that a property's "*true* market value" is a question of fact that is to be decided by the federal court using the best evidence available to it, even if that evidence points to an approach that diverges from the State's chosen method of valuation or demonstrates that the State's methodology is deeply biased or flawed. Moreover, as discussed below, a rule that rests on a purported distinction between method and application, allowing litigation of only the latter, would lead to unnecessary litigation and produce standardless and unpredictable decisionmaking regarding the question whether a particular challenge fell on one side or the other of that ephemeral line. The facts of this case amply demonstrate the weaknesses of such a rule.

B. The Text And Structure Of Section 11501 Demonstrate Congress's Intent That Federal Courts Determine True Market Value Based On The Best Evidence Available, Not Blind Adherence To State Methodologies

The text of Section 11501 demonstrates that Congress intended the federal courts to determine true market value using the best evidence available, even when that evidence departs from the State's various methodological choices. In *Burlington Northern*, the Court found the language of the 4R Act "clear" in requiring the federal courts "to determine what the 'true market values' are." 481 U.S. at 461. See *ibid.* (finding the legislative history "irrelevant" because "the terms of [the] statute [are] unambiguous") (quoting *Rubin* v. *United States*, 449 U.S. 424, 430 (1981)). Not only does the 4R Act's directive that federal courts independently determine "true market value" not distinguish between the State's choice of methodology and its application of that methodology—the latter of which is unquestionably subject to federal review, see *id.* at 462—it affirmatively indicates Congress's presumptive preference for using a particular methodology for deter-

mining true market value (*viz.*, a sales methodology) when feasible and satisfactory to the court, *regardless* of the method(s) preferred by the State.

Section 11501(c) provides that "[t]he burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. 11501(c). As the Court has recognized, "[i]t would be inconsistent to allocate the burden of proof as to an issue which could not be litigated in federal court in the first place." *Burlington Northern*, 481 U.S. at 462. Section 11501(c) goes on to provide that if satisfactory evidence is available, the federal court should generally utilize "the random-sampling method known as a sales assessment ratio study (to be carried out under statistical principles applicable to such a study)" to determine "the ratio of the assessed value of other commercial and industrial property in the assessment jurisdiction to the true market value of all other commercial and industrial property." 49 U.S.C. 11501(c). In other words, Congress concluded that arms-length sales that take place in the marketplace are presumptively the best evidence of "true market value," and it directed the federal courts to rely on such actual sales information whenever it can be used to determine the ratio of assessed to true market value of non-railroad commercial and industrial property "to the satisfaction of the district court." *Ibid.* Plainly, it would not be open to a State to object to such evidence on the ground that, for example, the State had determined the true market value of non-railroad commercial and industrial property using the income, rather than sales, method of valuation.

Section 11501(c) thus makes clear that Congress expected the federal courts to calculate the true market value of other commercial and industrial property by employing a sales-based approach whenever that method was satisfactory *to the district court*—and entirely without regard to the State's preferred method(s), if any, for making that determi-

nation. It logically follows that Congress's use of the same term—"true market value"—with respect to railroad property likewise refers to the value of the property as determined to the satisfaction of the district court without regard to the methodology utilized by the State. See *Powerex Corp.* v. *Reliant Energy Servs., Inc.*, 127 S. Ct. 2411, 2417 (2007) ("identical words and phrases within the same statute should normally be given the same meaning"). It is inconceivable, for example, that in light of Congress's expressed preference for sales information as evidence of true market value, Congress would have expected or intended that a State's methodological choices could preclude a court from considering the price at which a railroad was sold at the end of the previous year in determining its true market value.

The Court considered and rejected in *Burlington Northern* the argument that Section 11501(c)'s reference to a particular method for deriving the true market value of other commercial and industrial property implies, by negative inference, that Congress did not intend the federal courts to determine independently the true market value of railroad property. Rather, "the language of subsection (c) leads to the opposite conclusion." 481 U.S. at 462. The statute makes clear that "assessed value and true market value are subjects for judicial inquiry, and are to be proved," and the specific reference in subsection (c) to a method for proving the ratio for commercial property by a statistical sample is simply a "particular grant of authority * * * to use statistical methods." *Ibid.* It "raises no implication whatever that the value of another kind of property may not be proved at all." *Id.* at 463. By the same token, it raises no implication that a court is bound by the State's choice of methodology for valuing railroad property, but instead reflects Congress's expectation that federal courts would make a determination concerning "true market value," and that methodological choices, like

other aspects of that inquiry, would be matters for judicial resolution "to the satisfaction of the district court."

C. The Legislative History Likewise Reflects Congress's Understanding That State Assessments Would Be Measured Against A Federal Standard Of True Market Value, Rather Than The States' "Outdated Procedures"

The legislative history confirms that Congress did not intend to bind federal courts to the methodologies used by the States to evaluate railroad property. Indeed, the contrary intent is clearly reflected in the Senate Report's recognition that railroads "are discriminated against as compared to other property taxpayers in the same jurisdiction, due in large measure to *outdated procedures* (which are sometimes deliberately retained) for assessment of property." S. Rep. No. 630, 91st Cong., 1st Sess. 2 (1969) (emphasis added) (quoting Interstate Commerce Commission letter, which quoted the report on *National Transportation Policy*, S. Rep. No. 445, 87th Cong., 1st Sess. 451 (1961) (Doyle Report)). The Doyle Report noted that "[c]ost, whether it be original or reproduction cost, is poor evidence of system value for railroads," but that it nonetheless "remains in use" by States as a valuation method because "cost is usually a higher figure for railroads than current cash value." Doyle Report 456-457. By "justify[ing] a higher full value" for the railroad through the use of a cost methodology, a State could "in turn appear to produce a lower equalized assessment ratio." *Id.* at 457.[5] Plainly Congress did not forbid the federal courts to scruti-

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[5] The Second Circuit's decision in *Consolidated Rail Corp. v. Town of Hyde Park*, 47 F.3d 473, cert. denied, 515 U.S. 1122 (1995), exemplifies the cost methodology's potential to overvalue a railroad's property. In that case, the New York State Board of Equalization and Assessment, using a "cost approach," determined that Conrail's property in New York had a "true market value of $974 million," which was more than twice the $451 million value indicated by the "stock and debt" and "income capitalization" methods. *Id.* at 480.

nize those same valuation "procedures" that were the cause of the problem Congress sought to remedy.

The Senate Report further reflects the Committee's understanding that the statutory standard of "true market value" was to be the *federal* standard against which state assessments would be compared in determining discrimination. S. Rep. No. 630, *supra*, at 25-26; S. Rep. No. 1483, *supra*, at 22. The report indicates that the bill did not "require a State to change its assessment standards, assessment practice, or the assessments themselves," but that it did "provide[] a single standard"—true market value—"against which all affected assessments must be measured." *Ibid.* True market value "is not a standard for determining value; it is a standard to which values that have already been determined [*i.e.*, the State's assessments] must be compared." *Ibid.* Thus, "true market value" is not an assessment method or practice that the States were being required by Congress to adopt. States remain free to use any method they like in arriving at the numerator of assessed value. But the denominator of "true market value" is a federal standard as to which States are not owed particular deference. That remains true even if states calculate a market value or true market value as a step in their assessment. Their assessment, including any calculation of market value, is taken as a given for purposes of the numerator, but "true market value" in the denominator of Section 11501(b)'s ratio remains a question for the federal court. Indeed, as discussed at pp. 26-27, *infra*, some States do not even *attempt* to base assessments on true or fair market value. "True market value" is simply the *federal* standard to which state assessments are to be compared in determining whether a railroad has been subjected to discrimination. Plainly, "true market value" would not be much of a litmus test if the State's own assertions as to true market value were dispositive.

The court of appeals read the above-quoted statement from the Senate Report as "support[ing] the conclusion that rail-

roads may not challenge state valuation methodologies in federal court." Pet. App. 14a; *id.* at 40a-41a. But the assertion that States are not required to "change" their "assessment standards, assessment practices, or the assessments themselves," S. Rep. No. 630, *supra*, at 25, cannot plausibly be read to suggest that those matters—including "the assessments themselves"—are binding on the federal courts in the course of making their independent determinations of "true market value." The court of appeals' reading proves too much, as it would entirely nullify the Act (and overrule *Burlington Northern*) by forbidding any meaningful examination of true market value, at least in the many taxing jurisdictions that purport to "assess" at that value or a fixed proportion thereof.

Throughout the hearings leading up to the enactment of Section 306, state representatives repeatedly objected to an assessment-ratio test like the one ultimately adopted by Congress, on the precise ground that it would entail independent federal court determinations of value.[6] Notwithstanding those objections, Congress enacted the assessment ratio approach into law, signalling its rejection of those concerns. The legislative history thus confirms that Congress did not intend to limit the discretion of federal courts to employ valuation approaches different from those utilized by the States.

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[6] See *Discriminatory Taxation of Common Carriers: Hearings on S. 927 Before the Subcomm. on Surface Transp. of the Senate Comm. on Commerce*, 90th Cong., 1st Sess. 114 (1967) (statement of Charles F. Conlon); *State Tax Discrimination Against Interstate Carrier Property: Hearing on S. 2289 Before the Subcomm. on Surface Transp. of the Senate Comm. on Commerce*, 91st Cong., 1st Sess. 99, 102 (1969) (statement of George Kinnear).

II. THE RULE ADOPTED BY THE COURT OF APPEALS IS NEITHER WORKABLE NOR JUSTIFIED

A. The Court Of Appeals' Distinction Between Valuation Methodology and Application Is Ephemeral And Would Lead To Standardless Collateral Litigation

The approach adopted by the lower courts presupposes a meaningful and discernible distinction between a State's unreviewable choice of a valuation "methodology" and its reviewable "application" of that methodology. That purported distinction, however, is far too indeterminate and ephemeral to support the weight that the lower courts would place upon it. As the facts of this case demonstrate, valuation "methodology" and "application" are often indistinguishable in practice, and a rule that makes so much turn on the supposed distinction would only invite unnecessary and ultimately standardless collateral litigation about whether various aspects of the State's calculations fall on one or the other side of the line.

The rule adopted by the lower courts—that "[t]he district court was not allowed to consider a valuation methodology different from *the methodology* of the Board," Pet. App. 15a (emphasis added)—was based on the mistaken premise that "each appraisal is based on *a particular* methodology." *Id.* at 38a (emphasis added). See *id.* at 12a (deference to the State's "selection of a valuation methodology"). Valuation treatises make clear, however, that in general no single method of valuation produces a property's "true market value." Rather, an appraiser's ultimate estimate of value reflects evidence gathered from a variety of approaches (and techniques within approaches), the relative strength of which the appraiser weighs based on the particular facts and circumstances concerning the property. In most instances, there will be no single state "methodology" to which the court could defer.

"Appraisers develop an opinion of property value with specific appraisal procedures that reflect three distinct methods

of data analysis: 1. Cost[;] 2. Sales comparison[;] 3. Income capitalization." Appraisal Inst., *The Appraisal of Real Estate* 62 (12th ed. 2001) (Appraisal Inst.). None of those approaches (or variations on those approaches) yields, in itself, the property's "true market value"; rather, each provides an "indication of value," *i.e.*, "*evidence* of value." *Id.* at 597; Unit Valuation Report 3 (emphasis added). In any given appraisal, "more than one approach to value is usually applied, and each approach typically results in a different indication of value." Appraisal Inst. 597; James H. Boykin & Alfred A. Ring, Valuation of Real Estate 434 (4th ed. 1993) (Boykin) ("[T]he appraiser proceeds with an analysis of the data under each of the value approaches"). Indeed, "several value indications may be derived in a single approach," such as different indications of value derived "from applying income multipliers to specific types of income, directly capitalizing net income, and discounting cash flows." Appraisal Inst. 597.

The ultimate task of the appraiser is to reconcile the distinct indications of value generated by the different approaches to reach a final estimate of value. The process of reconciliation is not simply "a mathematical process involving mere averaging of the estimates derived under the independent value approaches." Boykin 434; see Appraisal Inst. 597-598. The appraiser's "task is to weigh the pertinency of such evidences and to make an objective analysis of each." Unit Valuation Report 59. "The appraiser weighs the relative significance, applicability, and defensibility of each value indication and relies most heavily on the approach that is most appropriate to the nature of the appraisal problem." Appraisal Inst. 600. The final opinion of value "need not be identical to the value produced by" any single approach. *Ibid.*

Thus, the lower courts' assumption that there will be a single "state methodology" to which to defer is mistaken. In any given appraisal, the State's final opinion of value often will not represent the figure that a single approach would

generate, but rather the appraiser's weighing of the different "evidences of value." That weighing process should reflect the appraiser's consideration of all the relevant facts, including the strength of the data upon which the calculations were derived and the nature of the property or enterprise being evaluated. Appraisal Inst. 600. It is impossible to discern where, in such a situation, the State's purportedly unreviewable "choice of methodology" ends and where its "application" begins.[7]

The facts of this case demonstrate the difficulty of identifying a principled basis for distinction. Here, it was undisputed that Georgia did not value all properties in Georgia, or even all centrally assessed properties, according to a single valuation approach. For each centrally assessed property, the State "calculat[ed] five values under three different methods and select[ed] a figure at the low end of the resulting range."

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[7] At the highest level of generality, when a State is making the initial determination whether to use the unit rule or the summation method to value railroad or other property, it may be fair to say that the choice is purely one of methodology, or perhaps even that it is part of the logically prior decision of what property the State is going to tax. One might argue that there is also a sufficiently clear methodological dichotomy between a "cost" approach, on the one hand, and an "income" or "sales" approach, on the other. See Unit Valuation Report 3 ("The cost approach is a summation appraisal, and as such may not be regarded as a measure of unit value."). Even at that level, however, the distinction becomes much less clear, because although cost is not itself an indication of unit value, it is "good information to guide judgment, and therefore is a proper evidence to consider in finding value." *Ibid.* As discussed above, most appraisers use a cost approach as just one of many evidences of value, with the final value opinion being derived from no one approach alone. There is even more practical overlap between the income and sales approaches, and moreover the choice of approach even at that high level of generality may reflect a fact-based assessment of the particular circumstances of the entity to be valued. In any event, there is simply no discernible line between "methodology" and "application" once the appraiser moves past the threshold question of cost, income, and/or sales methods and begins selecting sub-approaches (*e.g.*, DCF versus yield ratio), choosing techniques (*e.g.*, for determining a discount rate), and making assumptions and judgments based on the particular facts and circumstances.

Pet. App. 17a. The lowest figure could have been generated by the income approach in the case of one utility, by the stock and debt approach in the case of another, and by the market multiples approach in the case of a third. As the court of appeals recognized, in this case, the State's selection "of an appraisal amount nearest to the discounted cash flow number did not reflect the conclusion that discounted cash flow was the most accurate of the methods used, only that it was the lowest." *Id.* at 18a. It is at best awkward to describe the State's approach—always to choose the lowest of the calculated figures—as an "accounting method[]" or "valuation methodology" to which the courts must defer. And if deference is due here, it would seem equally applicable to a State's decision always to choose a particular method that is well-established to overvalue railroads relative to other commercial property.

The lower courts' refusal to consider the "yield capitalization" valuation proposed by petitioner's expert, Tegarden, on the ground that it was a different methodology from the State's DCF approach further demonstrates the difficulty of drawing the line that is at the heart of the court of appeals' rule. The district court recognized Tegarden's "yield capitalization" analysis as a "cousin" to the "discounted cash flow" analysis used by the State, because both are versions "of the income approach." Pet. App. 35a-36a. The court nonetheless concluded (and the court of appeals agreed, *id.* at 15a-18a) that Tegarden's was "a different valuation method" that could not be considered, *id.* at 45a.

That conclusion expands the scope of "methodology" into the realm of mere *assumptions* made by appraisers. While Dickerson and Tegarden expressed their respective approaches by different formulae, see Pet. App. 36a, the latter is simply a mathematical shorthand of the former if one assumes, as Tegarden did, that petitioner's income would remain level. See J.A. 80-81 (setting out Dickerson's DCF for-

mula, and noting that "[w]here income has the characteristics of a perpetuity * * *, the universal capitalization formula, *Value = Income ÷ Rate*, can be used").[*] Tegarden's calculations could likewise have been expressed in Dickerson's longer form, with the numerator remaining constant each year. Thus, the difference between the two formulae boils down to the appraisers' differing *assumptions* regarding the growth of petitioner's future income. An approach that deems appraisers' mere assumptions to qualify as unreviewable "methodology" would effectively preclude *any* meaningful review of state determinations of true market value, because the assumptions made by the appraiser at each step of the process ultimately determine the outcome of *any* valuation approach. See *Metlyn Realty Corp.* v. *Esmark, Inc.*, 763 F.2d 826, 835 (7th Cir. 1985) (Easterbrook, J.) ("It is a simple matter to increase or reduce the outcome of a cash flow analysis by 200% by making changes in assumptions [such as the firm's costs, rate of growth, and the discount rate] that appear by themselves to be insignificant.").

In an attempt to justify its conclusion that Tegarden's approach could not be considered, the court of appeals held that "all nonfactual determinations involved in constructing a valuation process, regardless of how broad or narrow they may be," qualify as "accounting methods" that a railroad may not challenge. Pet. App. 17a. In the first place, however, there is no basis for the court of appeals' view that an appraiser's particular assumptions about the best way to value a particular taxpayer's property are "nonfactual determinations"—surely the question whether a railroad's income should be held constant or assumed to increase in future years is more factual than legal in nature, as are most, if not all, of the myriad of

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[*] The district court's representation of Dickerson's discounted cash flow formula (Pet. App. 36a) contains an error. The court failed to compound the discount rate in each successive year. Under the correct formula, the denominator (1 + discount rate) should be squared in year two, cubed in year three, etc. See Appraisal Inst. 688.

other assumptions that appraisers must make in selecting, applying, and weighing various valuation approaches.

Under the court of appeals' rule, moreover, any valuation rule that a State can articulate in general terms would apparently become unassailable. For example, if the State were to adopt a general rule to treat property as obsolete only in certain circumstances, it could foreclose challenge to its refusal to make deductions for obsolescence for property that did not satisfy the rule as articulated by the State. Likewise, if the State adopted a "methodology" for determining the discount rate in DCF calculations, such as using the Federal Reserve Board's federal funds rate, that "nonfactual determination * * * in constructing [the] valuation process," Pet. App. 17a, would seemingly be immune from judicial scrutiny.

Plainly, the court of appeals' rule cannot be squared with this Court's holding in *Burlington Northern*, in which the Court specifically held that the district court could adjudicate petitioner's challenges to "the State's evaluation of the cost of capital" and its "refusal to make deductions for property which petitioner claims is obsolete." 481 U.S. at 463 n.5. Yet there is no other obvious place to draw a principled, meaningful, and judicially manageable line between that which is subject to judicial review and that which is not.

B. The Determination Of A Property's True Market Value Is A Common Judicial Function That The Courts Cannot Escape Under Section 11501

The court of appeals' reluctance to undertake judicial review of valuation methodologies reflects its view that such an inquiry would amount to inappropriate "freewheeling judicial second-guessing." Pet. App. 17a. The district court likewise believed that it was being asked to "dictate a particular valuation method to the Department," which it was not qualified to do. *Id.* at 42a. But the valuation of property is a function that courts routinely undertake, in numerous contexts. Moreover, because States need not make *any* attempt to calculate "true

market value" in the course of making property assessments, but instead can use an assessment formula driven by other factors, such as historical sales prices, courts applying Section 11501 will sometimes have no choice but to make an independent determination of "true market value," which *necessarily* will entail making determinations regarding methodology. The court's role in assessing "true market value" for purposes of the federal-law denominator is not materially different whether or not a State calculates market value as a step in its assessment process. The federal court's role under Section 11501 is not that of a state court deferentially reviewing administrative agency action; rather, it is to conduct a de novo hearing on whether the State has violated the railroad's federal right against de facto discrimination.

The federal courts are routinely called upon to decide questions of property valuation in contexts other than Section 11501. See, *e.g.*, *United States* v. *50 Acres of Land*, 469 U.S. 24, 29-30 (1984) (Just Compensation Clause); *VFB LLC* v. *Campbell Soup Co.*, 482 F.3d 624, 632 (3d Cir. 2007) (action in bankruptcy to set aside sale of corporate division as fraudulent); *Citicorp Real Estate, Inc.* v. *Smith*, 155 F.3d 1097, 1106 (9th Cir. 1998) (determination of property's fair value in suit for deficiency judgment); *McMurray* v. *Commissioner*, 985 F.2d 36, 40 (1st Cir. 1993) (valuation of land donated to charity in action for tax deficiency). There is no reason to believe that federal courts are any less competent to weigh expert testimony regarding valuation issues in litigation under Section 11501 than they are in those other contexts.

The courts below believed that Congress intended that federal courts *not* make determinations regarding valuation methodology pursuant to Section 11501(b)(1). To the contrary, however, by making a determination of "true market value" an essential component of any suit under Section 11501(b)(1), and without requiring States to undertake such a calculation, Congress plainly contemplated that the determi-

nation of value (which necessarily entails judgments regarding methodology) was one for the federal courts to make.

Although most States do determine some version of market value as part of their assessment processes, that is not necessarily the case. Historically, some taxing jurisdictions simply "estimate[d] the 'fractional' valuation directly without even attempting to first determine full value." Note, *Inequality in Property Tax Assessments: New Cures for an Old Ill*, 75 Harv. L. Rev. 1374, 1379 (1962); see *In re Kents 2124 Atl. Ave., Inc.*, 166 A.2d 763, 767 (N.J. 1961) (when "they valued new construction, the assessors expressly eschewed any conception of the value of the properties" in favor of drawing an "assessment" value directly from comparable properties); *Batson* v. *Pearl River County*, 35 S. 2d 712 (Miss. 1948) (upholding "arbitrary assessment value of $2.50 per acre" for "all cut-over lands in the county"). More recently, in *Nordlinger* v. *Hahn*, 505 U.S. 1 (1992), the Court upheld a state constitutional amendment that made it the express policy of the State *not* to tax properties as a percentage of their market value, but according to a formula based upon their historical value. *Id.* at 5-6, 18.

Actions under Section 11501 likewise illustrate that not all States calculate "true market value" within the meaning of the 4R Act. See, *e.g.*, *Louisville & Nashville R.R.* v. *Department of Revenue*, 736 F.2d 1495, 1499 (11th Cir. 1984) (holding that "full market value" rather than "just value" represents "true market value for purposes of section [11501]"). Cf. *Consolidated Rail Corp.* v. *Town of Hyde Park*, 47 F.3d 473, 476 (2d Cir. 1995) (noting New York's practice of assessing railroad property as a percentage of "taxable value," which differed from "true market value"). In fact, in the case at bar, the court of appeals recognized that the figure used by the State "did not reflect the conclusion that discounted cash flow was the most accurate of the methods used, only that it was the lowest." Pet. App. 18a. Thus, federal courts simply can-

not avoid their responsibility in an action under Section 11501(b)(1) to determine the railroad property's "true market value" for purposes of the federal statute.

Whereas the court of appeals would preclude review of the State's chosen methodology altogether, Pet. App. 15a, the district court attempted to chart a middle course, allowing review to determine whether the State's methodology is unreasonable or purposefully discriminatory. The district court's attempt to reintroduce a threshold element of discriminatory intent into Section 11501(b)(1) runs directly contrary to this Court's holding in *Burlington Northern*. Moreover, the district court's approach, which is analogous to the standard a court might apply in reviewing agency action, is inappropriate for a statute that creates a federal right against de facto discrimination by the State. The courts of appeals have recognized as much in selecting the appropriate standard of proof to govern claims under Section 11501. See *CSX Transp., Inc.* v. *Board of Public Works*, 95 F.3d 318, 323 (4th Cir. 1996) (action under Section 11501(b)(1) is "an original action" and "does not involve review of an assessment by a state agency or other comparable body"); *Burlington N. R.R.* v. *Bair*, 766 F.2d 1222, 1226 (8th Cir. 1985) (rejecting standard for administrative review in favor of that for "de novo review in state court"). But see *Burlington N. R.R.* v. *Department of Revenue*, 23 F.3d 239, 241 (9th Cir. 1994) (applying Washington's "clear, cogent, and convincing evidence" standard for review of tax assessments).[9]

[9] Section 11501(c) provides that the "burden of proof in determining assessed value and true market value is governed by State law." 49 U.S.C. 11501(c). Arguably, the reference to "burden of proof" refers to the question of which party bears the "burden," not to the separate question of the *standard* of proof that party must bear. Alternatively, if read as referring to the standard of proof, it should be the State standard for civil proceedings generally, not for assessment appeals. See *Bair*, 766 F.2d at 1226. Were it otherwise, a State might effectively immunize itself from challenge under Section 11501(b)(1) by imposing an impossibly high standard of proof on those who challenge assessments in its own courts. In any event, that question is not

Ironically, the approach adopted by the court of appeals grants state assessors more deference in an action under the 4R Act's anti-discrimination provision than they enjoy when their assessments are appealed to Georgia's own courts. As the Georgia courts have repeatedly held, "[j]ust and fair valuation of property is a question to be determined by the factfinder, [*i.e.*], the trial court." *Dougherty County Bd. of Equalization* v. *Casto Dev. Co.*, 491 S.E.2d 483, 485 (Ga. Ct. App. 1997). In the "de novo investigation" before the trial court, the burden is on the initiating party, but "neither party is entitled to any prima facia presumption regarding the correctness of its evidence of valuation." *Hirsch* v. *Joint City County Bd. of Assessors*, 463 S.E.2d 703, 705 (Ga. Ct. App. 1995) (citation omitted). Taxpayers may present the opinions of their own experts, who are free to offer testimony based on valuation methods different from those of the State. See, *e.g.*, *Casto Dev. Co.*, 491 S.E.2d at 484 (noting that taxpayer's expert had criticized "the county's cost approach" and offered his own multi-approach analysis that "ascribe[d] more weight to the income approach"). Like an action in Georgia court, an action in federal court under the 4R Act is a "de novo" proceeding, in which the railroad should be permitted to prove its claim of discriminatory taxation with any competent evidence.

C. The Court Of Appeals' Reliance On Concerns Of Federal Comity Is Misplaced

The court of appeals believed that its curtailment of federal court review was compelled by principles of federalism and respect for the States' sovereign interest in setting tax policy. Pet. App. 12a-13a. This Court rejected that argument in *Burlington Northern* and it should do so here as well.

In *Burlington Northern*, the State urged that "injunctive relief against state taxation offends the principles of comity."

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presented in this case because Georgia permits a de novo hearing, with no presumption in favor of the State's assessment or its valuation methodology. See p. 28, *infra*.

481 U.S. at 464 (citation omitted). The Court disagreed, explaining that while such "policy considerations * * * may have weighed heavily with legislators who considered the Act," the Court was "not free to reconsider them now." *Ibid.* The 4R Act itself, which creates an express exception to the Tax Injunction Act, 28 U.S.C. 1341, see 49 U.S.C. 11501(c), makes clear that Congress fully intended to authorize the federal courts to enjoin prohibited forms of discriminatory state taxation. Moreover, as *Burlington Northern* held, the statute unambiguously establishes "true market value" as an element of the railroad's federal claim that must be proved to the district court's satisfaction. 481 U.S. at 462-464. There is no basis for the court of appeals' insistence that Congress also specify in a "clear statement" (Pet. App. 14a) each element of "true market value" that the federal court is to determine.

The court of appeals believed that this Court's more recent decision in ACF, rather than *Burlington Northern*, was the more apposite, but its reliance on *ACF* was misplaced. There, the Court held that a State does not violate the 4R Act's prohibition against "another tax that discriminates against a rail carrier," 49 U.S.C. 11501(b)(4), when it exempts certain non-railroad property from a generally applicable ad valorem tax without providing a similar exemption for railroad property. 510 U.S. at 347-348. The Court reasoned that "[i]t would be illogical to conclude that Congress, having allowed the States to grant property tax exemption in subsections (b)(1)-(3), would turn around and nullify its own choice in subsection (b)(4)," which did "not speak with any degree of particularity to the question of tax exemptions." *Id.* at 343. By contrast, the statutory text and structure of Section 11501(b)(1) and (c) makes evident that Congress expected the federal courts to make an independent determination of "true market value," which includes considerations of methodology.

The court of appeals believed that *ACF*, rather than *Burlington Northern*, was more relevant because federal

review of the State's choice of valuation methodology is more intrusive than review of the State's application of that methodology. Pet. App. 11a-12a. In *ACF*, the Court stressed that "[p]roperty tax exemptions are an important aspect of state and local tax policy." 510 U.S. at 344. But the only "[i]mportant question[] of state policy" that the court of appeals identified regarding valuation methodologies was the possibility that a State would choose "a simple valuation methodology rather than a complicated one" due to budget constraints. *Id.* at 12a. There is no indication that Congress believed that a State's refusal to expend resources on an accurate appraisal should be a defense against a claim of de facto discrimination under the 4R Act. Indeed, among the problems that the Senate Report identified and to which the 4R Act was addressed were the States' "outdated procedures." S. Rep. No. 630, *supra*, at 2. Nor is there any reason to conclude that the State's "methodology" of choosing the lowest of five calculated values, or its fortuitous use of the discounted cash flow approach in this case, reflects an "[i]mportant question[] of state policy" that implicates the "fundamental power of the state." Pet. App. 12a.

CONCLUSION

The judgment of the court of appeals should be vacated.

Respectfully submitted.

PAUL D. CLEMENT
Solicitor General

PETER D. KEISLER
Assistant Attorney General

D.J. GRIBBIN
General Counsel
Department of Transportation

THOMAS G. HUNGAR
Deputy Solicitor General

DOUGLAS HALLWARD-DRIEMEIER
Assistant to the Solicitor General

ELLEN D. HANSON
General Counsel
Surface Transportation Board

ANTHONY J. STEINMEYER
ROBERT D. KAMENSHINE
Attorneys

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IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA; BART L. GRAHAM, AS COMMISSIONER OF REVENUE OF THE STATE OF GEORGIA; RUSSELL W. HINTON, AS STATE AUDITOR OF THE STATE OF GEORGIA; AND GENA L. ABRAHAM, AS DIRECTOR OF THE GEORGIA STATE PROPERTIES COMMISSION,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

BRIEF OF *AMICUS CURIAE* ASSOCIATION OF AMERICAN RAILROADS IN SUPPORT OF PETITIONER

OF COUNSEL:

LOUIS P. WARCHOT
JANET BARTELMAY
ASSOCIATION OF AMERICAN RAILROADS
50 F Street, N.W.
Washington, D.C. 20001-1564
(202) 639-2100

JULY 30, 2007

BETTY JO CHRISTIAN
Counsel of Record
TIMOTHY M. WALSH
MICHAEL A. VATIS
STEPTOE & JOHNSON LLP
1330 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 429-3000

Attorneys for Amicus Curiae Association of American Railroads

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INTEREST OF *AMICUS CURIAE*

The Association of American Railroads ("AAR") is a non-profit trade association that represents the Nation's major railroads. Its members are interstate rail carriers subject to the jurisdiction of the U.S. Surface Transportation Board.[1] They account for the great majority of rail freight business in the United States, employing 93% of the workers and generating approximately 95% of the freight revenues. AAR represents member railroads before courts, agencies, and the Congress in matters of common concern.

Rail carriers are among the oldest and most important instrumentalities of interstate commerce. The transportation of commodities from state to state over rail lines is critical to the Nation's economy and the national defense. Railroads carry hundreds of billions of dollars of goods each year, including shipments for the U.S. military services. Interstate rail traffic has increased substantially in recent years, and is expected to grow further as states, localities and shippers seek to shift freight from congested highways onto rail lines.[2] Class I railroads—the largest interstate rail carriers—paid over $558 million in property taxes in 2006.

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[1] Petitioner and Respondents have consented to the filing of this brief. Their mutual consent letter was filed with the Clerk on July 25, 2007. No counsel for a party authored this brief in whole or in part, and no party or its counsel made a monetary contribution intended to fund the preparation or submission of this brief (although Petitioner, which is a member of AAR, pays general membership dues).

[2] Shifting freight from highways to rail lines also provides economic and environmental benefits because railroads are substantially more fuel-efficient than trucks and produce less pollution. *See, e.g.*, STB Ex Parte No. 671, Statement of The Honorable Jeffrey N. Shane, Under Secretary for Policy, U.S. Department of Transportation 1, 7 (Apr. 11, 2007), *available at* http://www.stb.dot.gov/filings/all.nsf/457f7ba95a516a6285 2567d900574766/476d4f2 .6705be58852572b400013ac4/$FILE/218992. pdf.

AAR and its members have a vital interest in preserving the effectiveness of Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 (the "4-R Act"), now codified at 49 U.S.C. § 11501 (2000), and the federal remedies it provides.[3] Congress enacted Section 11501 to prohibit discriminatory state taxation of interstate railroads, a widespread and long-standing practice that it found to "unreasonably burden and discriminate against interstate commerce. . . ." 49 U.S.C. § 11501(b). On behalf of the railroad industry, AAR participated in the legislative process that led to passage of Section 11501 and has an important stake in ensuring that the reforms enacted by Congress are not lost or attenuated by permitting states to evade the protections Section 11501 provides.

The burden of discriminatory taxation would be harmful to interstate rail carriers, their shippers and consumers at any time. But it would be particularly harmful now, when railroads face the need to invest in major infrastructure upgrades to handle growing demand for service. Earlier this year, the Surface Transportation Board conducted hearings on capacity and infrastructure issues facing the industry. *See* Notice of Public Hearing, STB Ex Parte No. 671, Rail Capacity and Infrastructure Requirements, 72 Fed. Reg. 11,085 (Mar. 12, 2007). The Board described the market forces driving the need for increased rail infrastructure investment:

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[3] There are some differences in language between Section 11501 as originally enacted in Section 306 of Pub. L. No. 94-210, 90 Stat. 31, 54-55 (1976), and as subsequently recodified at 49 U.S.C. § 11503, which was later redesignated as 49 U.S.C. § 11501. The recodification was not intended to effect any substantive change. *Burlington Northern R.R. v. Oklahoma Tax Comm'n*, 481 U.S. 454, 457 n.1 (1987).

> In recent years, there has been growing recognition that rail capacity in the United States has become constrained. Those capacity constraints come at the same time as many forecasts predict that rail freight demands will continue to grow over the next twenty years. Railroads experienced a more than 50% increase in traffic from 1990 to 2003, and traffic is projected to continue to increase as the economy grows. Some forecasters predict that multimodal freight tonnage in the United States will rise by nearly 70% between 1998 and 2020.

Id. at 11,085 (footnotes omitted). As the Board went on to explain, "[t]he convergence of increased demand with constrained capacity has highlighted the need to address what further infrastructure investment will be required to meet these demands. *Id.*

AAR and a number of its members participated in those hearings, detailing the enormous capital investments that are required to meet the demand for additional rail service using new or upgraded infrastructure. AAR described the rapid rise of capital spending by the Class I railroads from $5.9 billion in 2003 to a projected $9.4 billion in 2007, as well as a wide range of major investments that those interstate carriers have recently made or will soon make.[4] The Department of Transportation also underscored the fact that

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[4] STB Ex Parte No. 671, Comments of the Association of American Railroads at 10-12 (Apr. 4, 2007), *available at* http://www.stb.dot.gov/filings/all.nsf/457f7ba95a516a62852567d900574766/f30e9ecaf18ade04852572b30064c1fd/$FILE/218972.pdf. Comments also were submitted by Burlington Northern Santa Fe Corporation, Canadian National Railway Company and its U.S. subsidiaries, CSX Corporation, Kansas City Southern Railway and affiliates, Norfolk Southern Railway Company, Union Pacific Corporation and Union Pacific Railroad Company.

"[f]reight railroading is among the most capital-intensive of industries," with continuing needs for major capital projects.[5]

The Eleventh Circuit's decision requiring courts to accept without question whatever methods state tax appraisers use to value railroad property vastly increases the potential for future state tax discrimination, and thus threatens to deter, limit or skew new rail infrastructure investment at the very time it is widely acknowledged as critical to the Nation's economy. That is precisely the sort of state-imposed obstacle to the movement of interstate commerce that Congress had the foresight to prohibit by enacting a comprehensive and permanent ban on state tax discrimination in Section 11501.

The concerns that motivated Congress to pass the 4-R Act thus are just as present today as they were in 1976. AAR and its members remain vitally interested in ensuring that the antidiscrimination measures Congress enacted are preserved and that railroads are permitted to offer all relevant evidence of state tax discrimination, as intended by Congress in Section 11501.

SUMMARY OF ARGUMENT

Congress enacted Section 11501 to end discriminatory state taxation of interstate railroads. Section 11501(b)(1), which is at issue here, prohibits states from taxing railroad property "at a value that has a higher ratio to the true market value of [such] . . . property than the ratio that the assessed value of all other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property." 49 U.S.C. § 11501(b)(1). In *Burlington Northern Railway v. Oklahoma*

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[5] Statement of Jeffrey N. Shane at 4-6, 8-10, *in* Ex Parte No. 671.

Tax Commission, 481 U.S. 454, 461 (1987) ("*Oklahoma Tax*"), this Court held that a railroad does not have to show discriminatory intent in order to challenge a state's valuation of its property. Rather, a railroad need only show that it was subjected to a higher assessment ratio than other commercial and industrial property. Moreover, the Court held that "in order to compare the actual assessment ratios," a district court must "determine what the 'true market values' are" on its own, and that "'true market value'" is *not* "whatever the State determines [it] to be. . . ." *Id.* at 461-62.

Oklahoma Tax left open the precise question presented in this case—whether Section 11501 bars courts from considering evidence of valuation methodologies different from the methodologies utilized by the state. But the plain language, structure and purpose of the statute, as well as the rationale of the Court's decision in *Oklahoma Tax*, all compel the conclusion that district courts are not precluded from considering, or determining true market value on the basis of, such evidence. The Eleventh Circuit's decision to the contrary imposes a judicially constructed exclusionary rule that prevents courts from considering all relevant evidence of true market value and undermines the statute's fundamental purpose. Such a holding would open a gaping loophole through which states would be able to engage in the very discriminatory practices Congress sought to prevent, permitting them to extract a disproportionate share of tax revenue from interstate railroads without fear of federal remedy.

ARGUMENT

I. Section 11501 Plainly Prohibits All Tax Discrimination by States, Including Discrimination Effected Through the Overvaluation of Railroad Property

A. Congress Sought to Prevent All State Tax Discrimination Against Interstate Rail Carriers

More than forty years ago, Congress recognized discriminatory state taxation as one of the key factors that had led to the drastic decline of the railroad industry. Special Study Group on Transportation Policies in the United States, Senate Comm. on Commerce, National Transportation Policy, S. Rep. No. 87-445 (1961). The problem became increasingly acute over the next decade, until Congress enacted the 4-R Act to address a host of problems that had left the railroad industry in a precarious financial condition and resulted in eight major railroad bankruptcies. S. Rep. No. 94-499, at 2-3 (1975), *reprinted in* 1976 U.S.C.C.A.N. 14, 15-16; H.R. Rep. No. 94-725, at 53 (1975). After 15 years of study, Congress enacted Section 11501 as a critical part of that reform. Its express intent was to end discriminatory state taxation of railroads.

Congress recognized that interstate railroads "are easy prey for State and local tax assessors." Discriminatory State Taxation of Interstate Carriers, S. Rep. No. 91-630, at 3 (1969). Interstate rail operations depend on enormous capital investments, which are essentially immovable; once constructed, those assets become captive to the taxing state. *See id.* Moreover, the normal political constraints that deter state officials from engaging in discriminatory or excessive taxation are absent when out-of-state railroads are forced to

bear that cost. *See id.* ("Railroads, oil pipelines, and other interstate carriers are nonvoting, often nonresident, targets for local taxation, and cannot easily remove their right-of-way and terminals.").

The nature of interstate railroad operations exacerbates the problem. Many operate across numerous states. Among the largest, the BNSF Railway system owns or operates rail lines in 28 states, the Canadian Pacific/Soo Line system 10 states, the Canadian National/Grand Trunk system 13 states, the CSX system 23 states and the District of Columbia, the Kansas City Southern Railway system 10 states, the Norfolk Southern system 23 states and the District of Columbia, and the Union Pacific system 25 states.[6]

The freight these systems and other interstate rail carriers move is often owned by, shipped from or shipped to customers outside states traversed in the rail movement. Intermodal traffic (the fastest growing segment) often begins or ends on motor carriers in states that are not included in the rail portion of the movement. And a substantial volume of interstate rail freight involves foreign commerce, carrying exports and imports to and from U.S. seaports as well as border crossings with Canada and Mexico. In many cases, rail freight may have no relation to a state other than passing through it while moving from its origin to its destination.[7]

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[6] *See* Schedule 702 of the Class I Railroad Annual Reports on Form R-1 for the year ending December 31, 2006, *available at* http://www.stb.dot.gov/econdata.nsf/f039526076cc0f8e8525660b006870c9?OpenView&Start=1&Count=300&Expand=1#1.

[7] This is true not only for railroads that have lines in more than one state, since railroads operating in a single state may nonetheless carry freight moving in interstate or foreign commerce.

The burden of a state's discriminatory taxation of interstate rail carriers thus does not necessarily—and indeed may never—fall on businesses or individuals in that state. When a state imposes discriminatory taxes on a railroad, the cost will be passed along to shippers to the extent competition and other forces permit, and from shippers to consumers. As Congress recognized, this shifts the cost of one state's discriminatory taxation to citizens of states that do not engage in tax discrimination: "Ultimately, the shipper and consumer pay the bill for discriminatory taxation. Not only are such taxes reflected in the transportation costs of goods purchased by the consumer, but also the consumers of States which do not discriminate are forced to share the cost of these burdensome tolls." S. Rep. No. 91-630, at 3.

The 4-R Act mandated an end to the historical burden of state tax discrimination and, with later legislation and regulatory reforms, paved the way for the railroad industry to recover, although that process took many years. But Congress was not merely focused on the past. The same structural incentives that had led states to impose discriminatory taxes on railroads historically—multistate movements by out-of-state railroads carrying freight that often merely transits the taxing state—remained in place. Congress therefore banned discrimination comprehensively, not only eliminating the specific modes of discrimination that burdened interstate rail traffic at that time, but also prohibiting all forms of tax discrimination that states might resort to in the future.

The necessity of doing so is evident. States appraise property with regular frequency. Opportunities for unlawful tax discrimination against railroads consequently may arise as often as each year. Ever-present budgetary concerns impel states to seek tax revenues wherever they appear to be available. Political constraints may contain that impulse as to

local taxpayers, but as Congress recognized, those constraints often do not apply when interstate railroads are the taxpayers. States thus face incentives on a regular basis to test the limits of Section 11501—and will surely pursue those incentives to the maximum extent possible if the Eleventh Circuit's rule permitting discrimination through the guise of valuation or accounting methodologies is allowed to stand.

Section 11501 was intended "'to put an end to the widespread practice of treating for tax purposes the property of [railroads] on a different basis than other property in the same taxing district.'" S. Rep. No. 91-630, at 2 (reference omitted). As originally enacted, it declares that it is an unreasonable and unjust discrimination against, and an undue burden on, interstate commerce for a state or political subdivision to engage in any of the following prohibited acts:

> (a) The assessment (but only to the extent of any portion based on excessive values as hereinafter described), for purposes of property tax levied by any taxing district, of transportation property at a value that bears a higher ratio to the true market value of such transportation property than the ratio which the assessed value of all other commercial and industrial property in the same assessment jurisdiction bears to the true market value of all such other commercial and industrial property.
>
> (b) The levy or collection of any tax based on an assessment which is unlawful under subdivision (a).
>
> (c) The levy or collection of any ad valorem property tax on transportation property at a tax rate higher than the tax rate generally applicable to other commercial and industrial property in the same assessment jurisdiction.

> (d) The imposition of any other tax which results in discriminatory treatment of a common carrier by railroad subject to this part.

Pub. L. No. 94-210, § 306, 90 Stat. 31, 54.

By barring state taxation of railroad property based on an assessed value that has a ratio to "true market value" higher than that for "other commercial and industrial property" and forbidding imposition of a higher tax rate than "generally applicable" to such other property, Section 11501 ensures that interstate railroads are treated no worse than the much larger population of business property owners—who have much greater influence on state tax policy decisions. With the last prohibition (subsection (d)), Congress imposed a catch-all ban on "any other tax" that yields discriminatory treatment of railroads. *See, e.g., Ogilvie v. State Bd. of Equalization*, 657 F.2d 204, 209 (8th Cir. 1981); *Union Carbide Corp. v. Indiana Bd. of Tax Comm'rs*, 161 F.R.D. 359, 364-65 (S.D. Ind. 1993) ("The 4-R Act was intended to combat all forms of discriminatory taxation of railroads.").

The very presence of subsection (d) (now Section 11501(b)(4)) emphatically confirms that Congress never intended to leave the enormous loophole in Section 11501(b)(1) the Eleventh Circuit has created. It would have been bizarre to allow discrimination effected through a state's choice of valuation methods but then broadly forbid "any other tax" (or as recodified, "another tax") that results in discrimination. The breadth of the catch-all makes clear both the comprehensive nature of the ban on discrimination Congress enacted and the repugnancy of the Eleventh Circuit's decision to that statutory scheme.

B. This Court in Oklahoma Tax Recognized that Section 11501 Requires Federal Courts to Determine for Themselves the "True Market Value" of Railroad Property

One method by which states have sought to discriminate against interstate railroads is by overvaluing their property. When a state overvalues a railroad's property, it nominally can apply the same tax rate as it does to other commercial and industrial property, and yet still exact more than the railroad's fair share of taxes. It is for this reason that Congress, in Section 11501, expressly prohibited states from assessing railroad property "at a value that bears a higher ratio to the true market value of such . . . property than the ratio which the assessed value of all other commercial and industrial property in the same assessment jurisdiction bears to the true market value of all such other commercial and industrial property."

This Court in *Oklahoma Tax* held that Section 11501 means what it says: the statute forbids a valuation of railroad property that is disproportionately high in relation to the property's true market value as compared with the valuation of other commercial and industrial property. 481 U.S. at 461. *Oklahoma Tax* explicitly confirmed that, in the event of a dispute, federal courts are responsible for determining a railroad's true market value. In order to perform the comparison of assessment ratios required under Section 11501, this Court decided, "it is necessary to determine what the 'true market values' are," *id.*, and therefore "assessed value and true market value are subjects for judicial inquiry," *id.* at 462. The Court squarely rejected the contention "that whatever the State determines the value of the railroad to be, the resulting assessment ratio is not subject to further judicial scrutiny . . . ." *Id.* at 461-62.

The Court did not then need to resolve whether a railroad may utilize a valuation methodology different from the state's appraiser when bringing a challenge under Section 11501, since the railroad used the same methodology as the state appraiser in that case and simply challenged the state's application of that methodology. 481 U.S. at 463 n.5. But the logic of the Court's decision compels the conclusion that railroads must be able to prove the true market value of their property using any methods that the district court finds more accurate than the state's approach. True market value is arrived at by applying several appraisal methods to various factual inputs. Thus, if, as this Court held, the true market value is subject to judicial scrutiny, courts must be allowed to consider whatever valuation methodologies are relevant to determining true market value.

Moreover, having courts consider all relevant evidence of valuation in Section 11501 cases—including different appraisal methods used in the valuation process—would not be unduly burdensome or complicated. District courts routinely weigh this sort of evidence in deciding the value of property in analogous cases.[8] Even under the Eleventh

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[8] *See, e.g., Suitum v. Tahoe Reg'l Planning Agency*, 520 U.S. 725, 742 (1997) ("determinations of market value are routinely made in judicial proceedings without the benefit of a market transaction in the subject property"); *United States v. Miller*, 317 U.S. 369, 374 (1943) (in condemnation proceedings, court's assessment of property's fair market value is the measure of just compensation); *Masayesva ex rel. Hopi Indian Tribe v. Hale*, 118 F. 3d 1371, 1378 (9th Cir. 1995) ("[W]e are not swayed by the argument that the 'fair value' determination is non-justiciable because it calls for a 'policy determination of a kind clearly for non-judicial discretion.' Congress already made the policy decision that the Navajo should compensate the Hopi. . . . What Congress left for the courts, calculating 'fair value,' is within the expertise of the judiciary."); *United States v. Tampa Bay Garden Apartments, Inc.*, 294 F.2d 598 (5th Cir. 1961) (detailing district court's consideration of valuation methods used by eminent-domain commission); *Horn v. McQueen*, 353 F. Supp. 2d 785 (W.D. Ky. 2004) (court carefully evaluated competing valuation

Circuit's constricted interpretation of the statute, courts would be obliged to review the application of the several valuation methods typically used by states' appraisers—just as the district court did here. Petition Appendix ("Pet. App.") at 34a-71a. Permitting courts to consider evidence based upon other methods thus would not result in an appreciably heavier burden on them.

Finally, there is little risk that permitting consideration of other methods would open the floodgates to valuation challenges. The very presence of Section 11501(b)(1), properly construed, deters discriminatory valuations of railroad property in the first place. In addition, many actions brought under Section 11501(b)(1) are settled before a district court is required to address valuation issues. Indeed, in the twenty years since this Court's decision in *Oklahoma Tax*, we are aware of fewer than a dozen reported decisions in which a district court undertook, acknowledged it would undertake or would have been required as a result of a remand to undertake an analysis of a railroad's true market value under subsection (b)(1).[9] Permitting courts to consider

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approaches of experts in ERISA case); *McKesson Corp. v. Iran*, 116 F. Supp. 2d 13 (D.D.C. 2000) (in determining damages, court carefully evaluated parties' direct-capitalization and discounted cash flow valuations of the affected business), *aff'd in part*, 271 F.3d 1101 (2001), *vacated in part*, 320 F.3d 280 (D.C. Cir. 2003); *Swope v. Siegel-Robert, Inc.*, 74 F. Supp. 2d 876 (E.D. Mo. 1999) (considering several stock valuation methods in case involving "squeeze-out" merger), *modified*, 243 F.3d 486 (8th Cir. 2001); *OMP v. Sec. Pac. Bus. Fin., Inc.*, 716 F. Supp. 251 (N.D. Miss. 1989) (in deficiency action, court considered five appraisal reports including three different valuation methods, and eventually adopted its own valuation approach); *United States v. 121.20 Acres of Land*, 333 F. Supp. 21 (D.N.C. 1971) (court considered four valuation methods for agricultural land).

[9] *See Union Pac. R.R. v. Utah*, 198 F.3d 1201 (10th Cir. 1999); *Burlington Northern R.R. v. Bair*, 60 F.3d 410 (8th Cir. 1995); *Consol. Rail Corp. v. Town of Hyde Park*, 47 F.3d 473 (2d Cir. 1995); *Burlington*

any valuation methods they deem relevant thus would preserve the salutary effects of the statute in preventing discrimination without overburdening the federal judiciary.

II. Requiring Courts to Value Property Using Only the Valuation Methods Used by the State's Appraiser Would Eviscerate This Court's Holding in *Oklahoma Tax*, Undermine the Statute's Purpose, and Create More—Not Less—Work for District Courts

If, in determining railroad property's true market value, district courts were limited to considering only the valuation methods used by the state's tax appraiser, this Court's holding in *Oklahoma Tax* would be rendered almost meaningless. Property appraisers can use a range of valuation methods and techniques to estimate market value, and typically use more than one in valuing a particular piece of property. Different methods may yield significantly different valuations, even when the underlying data is kept constant. The choice of methodology thus may have at least as great an impact on a valuation as the hard data. Yet, if courts were barred from considering any valuation methodology that was not used by the state's appraiser, states would be free to choose whatever methodology resulted in the highest valuation of a railroad's property, and district courts would be hamstrung in determining whether that valuation constituted the *true* market value of the property.

Northern R.R. v. Dep't of Revenue, 23 F.3d 239 (9th Cir. 1994); *Richmond, Fredericksburg & Potomac R.R. v. Forst*, 4 F.3d 244 (4th Cir. 1993); *Union Pac. R.R. v. Dep't of Revenue*, 920 F.2d 581 (9th Cir. 1990); *Burlington Northern R.R. v. James*, 911 F.2d 1297 (8th Cir. 1990); *Atchison, Topeka & Santa Fe Ry. v. Bd. of Equalization*, 795 F.2d 1442 (1986), *vacated and remanded*, 828 F.2d 9 (9th Cir. 1987) (*per curiam*); *Fox River Valley R.R. v. Dep't of Revenue of Wisconsin*, 863 F. Supp. 893 (E.D. Wis. 1994); *Union Pac. R.R. v. State Tax Comm'n of Utah*, 716 F. Supp. 543 (D. Utah 1988).

A court could certainly decide, in a particular case, that the state appraiser's methodology was the most likely to produce the best approximation of true market value. But this is by no means a given. A court can meaningfully make such a determination only after considering all relevant evidence and evaluating witnesses' credibility. Requiring a court to accept, without question, a state appraiser's methodology would turn the adversarial process into a one-sided show trial heavily slanted toward the state, and render the court a mere spectator or fact-checker. It would thus eviscerate this Court's unanimous and emphatic holding in *Oklahoma Tax* that true market value is a "subject[] for judicial inquiry," 481 U.S. at 462, and that true market value is not whatever the state says it is, *id.* at 461-62. *See also Monongahela Navigation Co. v. United States*, 148 U.S. 312, 327 (1893) (in condemnation proceedings, "determin[ing] what shall be the measure of compensation . . . is a judicial and not a legislative question," and it is not up to the legislature "to say what compensation shall be paid, or even what shall be the rule of compensation").

Such a result would also undermine the entire purpose of Section 11501. If a state appraiser's methodology had to be accepted by district courts without question, appraisers would be free to *purposely* employ methodologies that overvalued railroad property. It would be a bitter irony if, after this Court decided in *Oklahoma Tax* that a railroad need not prove that a state intended to discriminate in order to prevail under Section 11501, that statute were now interpreted in a way that *permits* intentional discrimination through a state's choice of methodology. Congress did not require proof of intent. But it also certainly did not mean to create a loophole that *immunized* intentional discrimination from judicial review.

The Eleventh Circuit's interpretation of Section 11501(b)(1) may, without cliché, be termed Kafkaesque. It amounts to holding that a district court must accept the state appraiser's valuation method in determining a railroad's true market value, even if that method in fact results in a demonstrably incorrect value. Unlike characters in Kafka novels, though, Congress—and this Court in *Oklahoma Tax*—meant what they said: "true" means true, not just what a state official deems necessary.[10]

The Eleventh Circuit's purported distinction (Pet. App. 16a) between "accounting methods" and "factual determinations" is also a false one—or at best a distinction that is exceedingly difficult to draw when it comes to property appraisals. For example, the cost methodology requires a determination of the amount by which assets have depreciated. But it is not clear whether, under the Eleventh Circuit's rule, resolution of this issue would be considered a factual determination, a methodological decision, neither, or some combination of the two. The reality is that valuations depend on a varying mix of methods, techniques, facts, and assumptions, with no easy distinction among the inputs to the process. *See, e.g.*, *United States v. Miller*, 317 U.S. 369, 374-75 (1943) ("[E]ven in the ordinary case, assessment of market value involves the use of assumptions, which make it unlikely that the appraisal will reflect true value with nicety. . . . [T]he application of this concept involves, at best, a guess by informed persons."); S. Rep. No. 91-630, at 15

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[10] *See* F. Kafka, *The Trial* (1925) ("it is not necessary to accept everything as true, one must only accept it as necessary"). The Eleventh Circuit's decision resembles that parable in *The Trial* in one other respect: just as the door-keeper to "the Law" tells a man waiting for admission that "this door was intended only for you" but refuses ever to admit him, the Eleventh Circuit tells railroads that Section 11501 created legal relief just for them, but then denies them meaningful access to that relief.

(Congress provided 5% "tolerance factor" to take into account the "uncertainties inherent in the assessment process"). To insist, as the Eleventh Circuit did, that "accounting methods" are off-limits to judicial inquiry but "factual determinations" are not is thus wholly at odds with the realities of property appraisals. *See, e.g., Burlington Northern R.R. v. James*, 911 F.2d 1297, 1301 (8th Cir. 1990) ("in cases like this the line between 'methodology' and 'application' is so thin as to be almost ephemeral."); *CSX Transp., Inc. v. Forst*, 777 F. Supp. 435, 443 (E.D. Va. 1991) (noting "[t]he real question presented, of course, is how one makes a distinction between 'method' and 'application.'").

Moreover, engrafting the Eleventh Circuit's distinction between valuation methods and factual determinations onto the statute would invite states to label anything they do in appraisals as being "methodology" and therefore immune from challenge—and the states can be expected to raise this issue in virtually every case. This would require district courts to expend judicial resources determining, as a preliminary matter, whether a railroad was using an accounting method different from the state's or whether it was only challenging the accuracy of the state's "factual determinations."[11] Yet that expenditure would not even be directed at the dispositive issue of true market value, thus wasting judicial resources without performing the role assigned to the courts by Congress.

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[11] This presumably would require the parties to present expert testimony (possibly by "experts" wholly independent of their appraisers) on the issue of what constitutes a part of the methodology and what constitutes a mere factual determination pursuant to the methodology.

III. Federalism Considerations Do Not Justify a Rule that Excludes Relevant Evidence of True Market Value and Effectively Immunizes Discrimination

The Eleventh Circuit concluded that a district court may not consider evidence of valuation that relies on an accounting method different from the state appraiser's because "[t]he text of the Act does not clearly state that railroads may challenge valuation methodologies." Pet. App. 14a. That conclusion was based on the Eleventh Circuit's mistaken view that a contrary result would impinge on state sovereignty. But allowing courts to consider different accounting methods does not intrude on state sovereignty. Even if it did, Section 11501 more than satisfies any "clear statement" rule.

A. District Court Consideration of Alternative Appraisal Methods in Determining True Market Value Would Not Intrude on State Sovereignty

The Eleventh Circuit's decision to apply the clear statement rule was predicated on the view that "[t]he selection of a valuation methodology is part of the fundamental power of a state" and involves "[i]mportant questions of state policy." Pet. App. 12a. But this premise misapprehends the nature of valuation decisions generally and is inconsistent with the facts of this case. As a rule, appraisers do not rely on one prescribed methodology when valuing property. Rather, depending on the characteristics of the specific property, the appraiser's experience, and the available data at hand, an appraiser normally utilizes several different methodologies. Each valuation method produces "evidence of value" which the appraiser then considers in his or her professional judgment. *See, e.g.*, National Ass'n of Tax Administrators, *Appraisal of Railroad and Other Public Utility Property for Ad Valorem Tax Purposes* 8 (1954). The

appraiser's choice of methodologies is an exercise of professional judgment about what price a property would bring if sold on the market—not the expression of legislative or executive policymaking.[12]

The facts of this case are consistent with this general approach. Georgia does not mandate any particular valuation methodology by state constitution or statute. Rather, the decisions on how to conduct the appraisal and select a final valuation of the railroad's property are largely left to appraiser discretion. *See* Pet. App. 3a-5a. Indeed, Georgia appraisers made significant changes in their methodological approach from year to year, and even in the course of developing and defending the valuation at issue in this case. *Id.*[13] These repeated and *ad hoc* changes by individual appraisers belie the notion that the choice of valuation methods is such a fundamental expression of state policy that it should be immune from judicial inquiry. Moreover, Georgia counties are not even required to use the State

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[12] This case thus differs markedly from *Department of Revenue v. ACF Industries*, 510 U.S. 332 (1994). There, this Court, interpreting subsection 11501(b)(4) (the statute's "catch-all" provision), noted that principles of federalism supported its interpretation of the provision as not prohibiting states from granting tax exemptions for non-railroad properties. In that case, however, the state exempted by statute various classes of business property as a matter of legislative policy.

[13] Georgia had used the yield capitalization approach—the same approach on which CSX's expert primarily relied in this case—in prior years, but in 2002 a new appraiser switched methodologies. That switch was not the result of any state policy pronouncement. Rather, appointment of a new appraiser led to a change in methodology, and that new appraiser himself made further changes during the course of this litigation. *See* Pet. App. 3a-5a. In addition, the state's appraiser ultimately settled on a valuation "at the lower end of the range" produced by his different methods in order "to avoid litigation," not because of any state "policy" favoring one method over another. Pet. App. 5a.

appraiser's proposed assessment for public utilities. Pet. App. 2a-3a. Thus, different appraisers in each relevant Georgia county could have used their own methodologies to assess the value of CSX property in each county, and the counties could have used those valuations rather than the state appraiser's in levying taxes.[14]

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[14] This consequently is not a case in which a particular methodology was mandated or precluded by a state's constitution or statutes. *Compare Chesapeake W. Ry. v. Forst*, 938 F.2d 528, 529-30 (4th Cir. 1991) (Virginia constitution precluded use of unit valuation); *Arizona v. Atchison, Topeka & Santa Fe R.R.*, 656 F.2d 398, 400 (9th Cir. 1981) (state statute requiring railroads to be assessed at 60% of full cash value and most other commercial and industrial property at 50%). But whether or not a methodology is embodied in constitutional or statutory provisions is beside the point. If such provisions require discrimination against railroads, they violate Section 11501. *See, e.g.*, S. Rep. No. 91-630, at 9 (discriminatory "actions are forbidden under the language of [the bill] whether they are taken pursuant to or in accordance with a State constitutional provision or State or local statute, or administrative order or practice, or otherwise"). Insulating constitutional or statutory valuation rules from challenge thus would be directly contrary to Section 11501. It also would invite states to enshrine discrimination in those forms. *Cf Louisville & N. R.R. v. Pub. Serv. Comm'n*, 493 F. Supp. 162, 166 (M.D. Tenn. 1978) (amendment to Tennessee Constitution requiring railroads to be assessed at 55% of value, but industrial and commercial property at 40%, adopted after discriminatory appraisals were held to violate Equal Protection Clause) (prior to effective date of Section 306), *aff'd*, 631 F.2d 426 (6th Cir. 1980). Although a state constitution or statute may bind state appraisers, it does not bind a federal court applying a federal statute. *Cf. Miller*, 317 U.S. at 379-80 ("We need not determine what is the local law [for determining fair market value], for the federal statutes upon which reliance is placed require only that, in condemnation proceedings, a federal court shall adopt the forms and methods of procedure afforded by the law of the State in which the court sits. They do not, and could not, affect questions of substantive right—such as the measure of compensation—grounded upon the Constitution of the United States." (footnotes omitted)).

Even if a state appraiser's choice of valuation methods could be characterized as an expression of policy or an exercise of fundamental state sovereignty, allowing courts to consider other methods in determining true market value does not infringe on that sovereignty. Nothing in Section 11501 requires that a state's appraiser forsake his or her preferred valuation methods and adopt one chosen by a federal court. Rather, the statute simply prevents a discriminatory *outcome*, regardless of the methodology the state's appraiser employs, and provides a remedy where a court finds discrimination that exceeds a certain threshold.[15] Moreover, the remedy provided by Section 11501 is not to impose some uniform federal valuation method, but merely to enjoin the amount of taxation that resulted from discrimination—*i.e.*, the amount above what would have been required if the railroad's property had been assessed fairly, and consistently with other commercial and industrial properties. The original text of Section 11501(b)(1) as enacted prohibited assessment discrimination "only to the extent of any portion based on excessive values as hereinafter described." *See* Pub. L. No. 94-210, § 306(1)(a), 90 Stat. 31, 54 (1976); *see also* S. Rep. No. 91-630, at 13.[16] The state appraiser can continue to use whatever valuation method he or she chooses, subject only to the requirement that it not result in unlawful discrimination against the railroad. (And those methods might produce nondiscriminatory results for other taxpayers or in other years.) The statute thus in no way proscribes or prescribes any particular methodology.

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[15] *See, e.g.*, S. Rep. No. 91-630, at 25-26 ("[The bill] does not suggest or require a State to change its assessment standards, assessment practice, or the assessments themselves. It merely provides a single standard against which all affected assessments must be measured in order to determine their relationship to each other.").

[16] The deletion of that phrase occurred in recodification, which was not intended to make any substantive change in the law.

To the extent Section 11501 might impinge on state sovereignty interests, such impingement arises from the fact that the statute allows a railroad to contest, and courts to review, a state's valuation of property in the first place. But as this Court concluded in *Oklahoma Tax*, while "[t]hese are policy considerations which may have weighed heavily with legislators who considered the Act and its predecessors," they are not reason for a court to refuse to enforce the statute's plain meaning. 481 U.S. at 464. Thus, this Court unanimously affirmed a court's ability, and responsibility, to determine true market value. Allowing courts to consider different appraisal methods in making that determination of true market value in no way constitutes an additional impingement on state sovereignty. It simply permits courts to consider, in the normal and regular course of conducting the judicial inquiry upheld in *Oklahoma Tax*, all relevant evidence. Nothing in the statute suggests that a state appraiser's choice of methodology is immune from review, or that courts must exclude certain evidence that contradicts a state appraiser's valuation. The Eleventh Circuit's decision to the contrary creates a judicially engrafted exclusionary rule that undermines congressional intent and impedes district courts from performing their traditional role of considering all relevant evidence.

B. Even if a Clear Statement of Congressional Intent to Allow Consideration of Alternative Valuation Methods Were Required, Section 11501 Is Amply Clear

Even if a "clear statement" of congressional intent were required, Section 11501 is more than clear. In *Oklahoma Tax*, this Court held that Section 11501's plain language clearly "permits review by federal courts of alleged overvaluation of railroad property by state taxation

authorities." 481 U.S. at 456. Seven years later, in *ACF Industries*, this Court noted that the "reach of subsections (b)(1)-(3) is straightforward," 510 U.S. at 337, and that "Congress prohibited discriminatory tax rates and assessment ratios in no uncertain terms and set forth precise standards for judicial scrutiny of challenged rate and assessment practices," *id.* at 343 (citations omitted). Nothing in those decisions suggested that Congress's certain and precise language in fact contained some hidden ambiguity that would gut the entire purpose of the statute.

Congress was well aware when it enacted Section 11501 that appraisers use different methodologies to estimate the market value of property. *See, e.g.*, S. Rep. No. 91-630, at 4, 25 (noting varying assessment practices of states and localities, and the resulting variation in valuations). Congress was also well aware that courts routinely make independent determinations of market value, in tax assessment as well as condemnation and other cases.[17] Such determinations necessarily require a decision as to what valuation methods to employ.[18] Congress therefore knew

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[17] The legislative history of Section 11501 includes citations of cases in which courts evaluated the different methodologies employed by the parties in order to determine the market value of the property in question. *See* S. Rep. No. 91-630, at 25 (*citing New York Bay R.R. v. Kelly*, 22 N.J. Misc. 204, 37 A.2d 624 (N.J. B.T.A. 1944); *Fort Worth & D.N. Ry. v. Sugg*, 68 S.W.2d 570 (Tex. Civ. App. 1934); and *Guyandotte Valley Ry v. Buskirk*, 57 W. Va. 417, 50 S.E. 521 (1905)). Congress must also be presumed to be aware of this Court's numerous decisions holding that courts must assess all relevant evidence in determining a property's market value. *See, e.g., Miller*, 317 U.S. at 374; *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 327 (1893).

[18] *See, e.g., Guyandotte Valley Ry.*, 50 S.E. 521 ("numerous witnesses were introduced and examined in support of the contentions [of the parties]" and "[t]wo inconsistent theories, respecting the measure of compensation . . . were presented" to the court), *cited in* S. Rep. No. 91-630, at 25). Even the district court below acknowledged that "[i]n a more

that courts, in determining true market value under the "precise standards" of Section 11501, would need to decide which methodologies would produce the best estimate of true market value in a particular case. Indeed, it would have been superfluous for Congress to have explicitly instructed courts to consider all relevant evidence in determining true market value, including evidence concerning different valuation methods. Such a direction goes without saying. To paraphrase *ACF Industries*, 510 U.S. at 344, given the prevalence of judicial assessment of valuation methodologies when Congress enacted the 4-R Act, Section 11501's silence on the subject of methodologies simply reflects a determination to let courts use the normal methods of determining value.

Moreover, Congress specifically provided that the burden of proof in determining true market value is governed by state law. 49 U.S.C. § 11501(c). This shows that Congress knew how to put limits on how true market value could be proven when it wanted to. Yet, notably, it did not choose to put any such limit on what valuation methodologies railroads could use or courts consider. *See id.*

Finally, interpreting the statute as *not* permitting courts to consider alternative valuation methodologies would result in a situation "so bizarre that Congress could not have intended it." *ACF Industries*, 510 U.S. at 347 (internal quotation marks omitted) (*quoting Demarest v. Manspeaker*, 498 U.S. 184, 191 (1991)). It would mean that Congress established a broad and comprehensive prohibition against discriminatory taxation of railroads and a remedial scheme that permits courts to determine the true market value of railroads, but

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typical case, the court would look to both [the railroad's] appraisal and the Department's appraisal to determine the true market value of CSXT." Pet App. 37a n.8.

that Congress then "turn[ed] around and nullif[ied] its own choice" by precluding courts from considering evidence regarding one of the most critical elements used to determine value—the valuation method. *Id.* at 343. Such a result would simply be "untenable in light of §[11501] as a whole." *Id.*

CONCLUSION

For the foregoing reasons, the judgment should be reversed and the case remanded for a new trial.

Respectfully submitted,

OF COUNSEL:

LOUIS P. WARCHOT
JANET BARTELMAY
ASSOCIATION OF AMERICAN RAILROADS
50 F Street, N.W.
Washington, D.C. 20001-1564
(202) 639-2100

BETTY JO CHRISTIAN
Counsel of Record
TIMOTHY M. WALSH
MICHAEL A. VATIS
STEPTOE & JOHNSON LLP
1330 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 429-3000

Attorneys for Amicus Curiae Association of American Railroads

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IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,
Petitioner,

v.

STATE BOARD OF EQUALIZATION
of the State of Georgia; Jerry Jackson, as Commissioner of Revenue of the State of Georgia; Russell W. Hinton, as State Auditor of the State of Georgia; and Ray J. Crawford, as Director of the Georgia State Properties Commission,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

BRIEF OF *AMICUS CURIAE* COUNCIL ON STATE TAXATION IN SUPPORT OF PETITIONER

STEPHEN P. KRANZ *
DOUGLAS L. LINDHOLM
JANA MALONE
BOBBY L. BURGNER
J. HUGH MCKINNON
COUNCIL ON STATE TAXATION
122 C Street, N.W., Suite 330
Washington, D.C. 20001
(202) 484-5221

* Counsel of Record

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D.C. 20002

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BRIEF OF *AMICUS CURIAE* COUNCIL ON STATE TAXATION IN SUPPORT OF PETITIONER

INTEREST OF *AMICI CURIAE*

This brief *amicus curiae* in support of petitioner is filed on behalf of the Council On State Taxation ("COST").[1] COST is a non-profit trade association formed in 1969 to promote

[1] No counsel for a party authored this brief in whole or in part, and no person or entity other than *amicus curiae* has made a monetary contribution to the preparation or submission of this brief. Written consent of all parties to the filing of this brief has been filed with the Clerk of this Court.

equitable and nondiscriminatory state and local taxation of multi-jurisdictional business entities. COST represents nearly 600 of the largest multistate businesses in the United States; companies from every industry doing business in every state. While COST's membership includes the major railroad providers, which will be directly impacted by an interpretation of the statutory provision at issue, our broader company membership is concerned about the ramification this case will have on the validity and effectiveness of many other federal laws protecting interstate commerce from discriminatory and unduly burdensome state taxation.

STATEMENT OF THE CASE

In 2002, an appraiser working for the Property Tax Division of the Georgia Department of Revenue adopted a new valuation method to determine the property tax assessment to be made against CSX Transportation, Inc. (CSX). That new method resulted in a 41.3% increase in CSX's tax liability for the year and subjected CSX's property to a higher level of tax than other commercial and industrial property in the State.

CSX challenged Georgia's 2002 discriminatory assessment under Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act" or "the Act"), 49 U.S.C. § 11501 (2002), bringing suit in the United States District Court for the Northern District of Georgia. The suit alleged that Georgia had violated the 4-R Act by assessing the property of CSX at a higher ratio of its true market value than the ratio of assessed value to true market value of other commercial and industrial property, exceeding the 5% threshold in the Act.

The United States District Court for the Northern District of Georgia found that the 4-R Act barred consideration of valuation methodologies different from the methodology used by the State. Instead the court sought to narrowly construe the Act to allow only challenges to the factual determinations

made in employing the state's methodology. A panel of the United States Court of Appeals for the Eleventh Circuit upheld the District Court's decision.

This Court granted certiorari and the parties are briefing the following question: whether, under the federal statute prohibiting state tax discrimination against railroads, 49 U.S.C. § 11501(b)(1), a federal district court determining the "true market value" of railroad property must accept the valuation method chosen by the State.

SUMMARY OF ARGUMENT

For the 4-R Act to have meaning it must be applied to allow taxpayers to litigate the ultimate question relevant to determine whether discrimination exists, that is: what is the true market value of rail transportation property? In turn, litigating this question must, to be effective, encompass an adjudication of the appropriate method necessary to determine the true market value. The Eleventh Circuit's decision to limit litigation to factual components of a state selected methodology neuters the litigation by artificially restricting the challenge to a set of questions that are not necessarily, or even likely, dispositive of the question to be asked under the 4-R Act itself.

The Eleventh Circuit inappropriately applied the clear statement rule to justify its conclusion that Congress did not intend to allow federal courts jurisdiction over matters of state property tax valuation methods. The 4-R Act is unambiguous in its intent to identify and eradicate discrimination against railroad property. It does so in a manner that balances federalism interests while clearly granting taxpayers the ability to challenge discrimination in federal court. The Eleventh Circuit's conclusion that the district court should have jurisdiction over the issue of value but not have the ability to adjudicate how value is determined is a queer reading of the straightforward charge of § 11501. Congress

here did make a clear statement; district courts are able to fully adjudicate challenges to value, including how those values are calculated; the Eleventh Circuit erred in determining that the clear statement rule is violated.

Indeed, the Eleventh Circuit's broad application of the clear statement rule could jeopardize many other federal statutory provisions governing state and local tax. Serving in its role as the protector of interstate commerce, Congress has intervened in the world of state taxation numerous times to establish rules for, clarify, and foster uniformity in state tax treatment of multistate transactions and enterprises. Unless the decision below is corrected, each of these statutory provisions could be put into question by the Eleventh Circuit's broad application of the clear statement rule.

ARGUMENT

I. FAILURE TO READ 49 U.S.C. § 11501(b) & (c) TO GRANT FEDERAL DISTRICT COURTS THE ABILITY TO ADJUDICATE THE METHODOLOGY BEHIND PROPERTY VALUATION WOULD EVISCERATE THE FUNDAMENTAL PURPOSE BEHIND THE STATUTE.

Tiring of complaints regarding "studied and deliberate"[2] state discrimination against railroads, Congress passed the Railroad Revitalization and Regulatory Reform Act in 1976 ("4-R Act" or "the Act"), 49 U.S.C. § 11501 (2002). The Act specifies four prohibited activities which, if done by a state or local taxing authority, are considered to be discriminatory and an unreasonable burden on interstate commerce. The Act does not allow states or localities to:

> (1) Assess rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed

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[2] S. Rep. No. 87-445, at 458 (1961).

value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.

(2) Levy or collect a tax on an assessment that may not be made under paragraph (1) of this subsection.

(3) Levy or collect an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.

(4) Impose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the Board under this part.

49 U.S.C. § 11501(b).

The purpose of these four prohibitions is clear from their language: to prohibit discrimination caused by inflating railroad property assessed values (compared to their true values); to prohibit the levy or collection of tax based on these inflated values; to prohibit discrimination by imposing higher tax rates on railroad property; and to prohibit any other tax that discriminates against railroads. Of these four prohibitions only the first, and Congress' intention in that regard, is relevant to the present case.

Congress sought by § 11501(b)(1) to prohibit sub-national tax jurisdictions from taxing railroad property at a higher value than the tax imposed on non-railroad property. In crafting a statutory formula to determine whether the taxing authority had engaged in discrimination against railroads, Congress chose a comparison approach to see if disparity exists between treatment of railroad and non-railroad property. To make the comparison, one must evaluate the assessed value of railroad property against its true market value. The assessed value is self apparent; determining the true market value is the heart of the investigation and resulting dispute.

As set forth thoroughly in the Brief of Petitioner (pp.6-12), there are numerous methods and combinations of methods which can be used to calculate the true market value for purposes of taxation of property. Because the different valuation methodologies serve different purposes in the valuation process, the use of a method inappropriate to the specific property use or type can produce a valuation that is inapplicable to the actual property involved in the dispute. Using the incorrect method will produce a value that is correct for the method but incorrect for the property. For § 11501(b)(1) to have meaning, and for the formula comparison to be applied effectively by the district court, the court must have the ability to look at the state's chosen methodology to determine whether it is the appropriate method to use given the type and use of the property in question.

Said another way, to evaluate a taxpayer's claim of discrimination under § 11501(b)(1), the Act must anticipate that the district court will reach a decision on each of the elements included in the basic formula laid out in § 11501(b)(1). Those elements include determining the assessed value of the railroad property; the true market value of the railroad property; the assessed value of other commercial/industrial property; and the true market value of the other commercial/industrial property.

The purpose of making these four determinations is so that the railroad property ratio can be compared with the commercial/industrial property ratio. If the railroad ratio exceeds by at least five percent the ratio for commercial/industrial property, the state's assessment violates the 4-R Act and the district court is granted jurisdiction to provide relief. 49 U.S.C. § 11501(c).

This Court recognized the fundamental purpose of § 11501 in *Burlington Northern Railroad v. Oklahoma Tax Commission*, 481 U.S. 454 (1987), where it determined that the statute "permits review by federal courts of alleged over-

valuation of railroad property by state taxation authorities" and recognized that the statute was "Congress' solution to the problem of discriminatory state taxation of railroads." *Id.* at 456-457.

Congress' solution included granting taxpayers the ability to challenge alleged discrimination in the district courts of the United States. While taxpayers have always had the ability to challenge discrimination in their local court system, Congress concluded that the local court systems had proven too biased to effectively address the discrimination and that it was appropriate for Congress, under its express Commerce Clause authority, to put the issue of discriminatory valuation in front of a federal judge. This decision, because of its impact on the federal-state relation, was not made lightly and should not be judicially re-written as has been done by the Eleventh Circuit.

While this Court has previously addressed 4-R Act cases, it specifically noted that it had not addressed the question presented today, stating in *Oklahoma Tax Commission*, "[t]his case therefore does not present the question whether a railroad may, in an action under § 11503 [now § 11501], challenge in the district court the appropriateness of the accounting methods by which the State determined the railroad's value, or is instead restricted to challenging the factual determinations to which the State's preferred accounting methods were applied. Accordingly we express no view on that issue." *Id.* at 463. The Court however otherwise made clear that "assessed value and true market value are subjects for judicial inquiry." *Id.* at 462.

Unfortunately, the Eleventh Circuit's narrow approach to the statute would prevent the district court from determining the true value of the railroad property by prohibiting the district court from looking behind the methodology to determine the appropriate valuation for ratio comparison. This approach results in an interpretation of the 4-R Act that says taxpayers may challenge the value but may not prove that the

value is incorrect. To the listening taxpayer community, the Eleventh Circuit's hollow challenge has the sound of one hand clapping – it sounds to be no challenge at all.

The correct approach was articulated by Judge Fay in his dissent from the Eleventh Circuit's opinion. Judge Fay wrote that, "[t]he language of the statute is straightforward and prohibits states from assessing rail transportation property at a value that has a higher ratio to the true market value than the ratio that the assessed value of other commercial and industrial property has to its true market value." *CSX Transportation, Inc., v. State Board of Equalization*, 472 F.3d 1281 at 1292 (2006). Judge Fay concluded that the objective of any methodology utilized is a determination of true market value and therefore taxpayers should be allowed to challenge the methodology if they can establish that it results in an unacceptably higher tax ratio for railroad property. *Id.* at 1294. The Eleventh Circuit's majority approach instead relegates taxpayers to disputing factual differences with the state's application of its chosen methodology, an exercise which largely blesses the manipulation (and resulting discrimination) that stems from selection of the methodology itself. It is the adoption of valuation methods, not just factual misapplication, that leads to distorted valuation of railroad property. As Judge Fay recognized in his dissent, "if the Act were to be interpreted, [to eliminate methodology challenges], so that the [state] could adopt a special appraisal method for railroads alone, then the whole nondiscrimination objective of the statute could be circumvented." *Id.* Preventing the district court from investigating the resulting distortion is tantamount to blessing it, a decision clearly at odds with the Congressional intent.

This Court's history with the Act supports an interpretation which would give the district court authority to evaluate the underlying methodology. In *Oklahoma Tax Commission*, the state took the position that whatever "the State determines the

value of the railroad to be, the resulting assessment ratio is not subject to further judicial scrutiny in the federal courts." *Okla. Tax*, 481 U.S. at 462. This Court found the state's restrictive thinking (identical in nature to that espoused by Georgia in the present case), to be inconsistent with language in the Act; the Act specifically allocates the burden of proof in determining "assessed value and market value [as] governed by State law." *Id.* Similarly here, the allocation of burden of proof on the question of market value supports the view that district courts were granted jurisdiction to fully determine market value, an exercise which by its nature includes an exploration of the methods involved in determining market value.

II. THE ELEVENTH CIRCUIT MISAPPLIED THE CLEAR STATEMENT RULE.

The Eleventh Circuit misapplied the clear statement rule, relying on this Court's holding in *Department of Revenue v. ACF Industries, Inc.*, 510 U.S. 332 (1994). This Court's ruling in *ACF* does not, as was found to be the case by the Eleventh Circuit, apply to prohibit challenges to valuation methods under § 11501(b)(1). *ACF Industries* involved application of § 11501(b)(4), which prohibits imposition of a separate "tax that discriminates against a rail carrier." 49 U.S.C. § 11501(b)(4). ACF sought to challenge the state's allowance of property tax exemptions for nonrailroad property when such exemptions were not allowed on railroad property. The Court evaluated the taxpayer's argument that the 4-R Act prohibited the state from granting property tax exemptions to nonrailroad property without granting them to railroad property and held that such challenges were not allowed under the Act. This Court's holding in *ACF* can be summarized as prohibiting challenges to property tax exemptions under the 4-R Act because Congress did not express a clear intent to allow such challenges. *ACF Industries*, 510 U.S. at 345.

The present case, on the other hand, involves a straightforward challenge to a discriminatory tax assessment under § 11501(b)(1), raising for consideration the fundamental purpose of the anti-discrimination statute. Unlike the decision in *ACF* where the statutory language never once goes so far as to mention property tax exemptions, Congress expressly raised the question of valuation in the statute. It cannot be believed that challenges to value and the methods used to calculate value were not the clear and manifest purpose of Congress in adopting the language in § 11501(b)(1).

The Eleventh Circuit's application of the clear statement rule to § 11501(b)(1) was based on the fact that "[t]he text of the Act does not clearly state that railroads may challenge valuation methodologies." *CSX Transportation*, 472 F.3d at 1289. It is true that the word methodologies itself does not appear in the statute, but the statute forces a consideration of those methodologies through § 11501(c) which requires the district court to determine whether the state has violated the assessment to market value formula in determining whether the state has engaged in discrimination. Making this determination requires that the court reach a conclusion regarding the true market value of the railroad property. The court cannot make this necessary finding without exercising the ability to evaluate the methodology as an inherent part of the true market value determination. To determine true market value one must consider the underlying facts as well as the method chosen to apply those facts. Eliminating the methodology analysis from the litigation has the impact of limiting the district court to checking on whether the parties have accurately counted the number of track miles or other mundane factual details which are relatively inconsequential in the overall valuation process. Congress could not have intended for its statute prohibiting value based discrimination to not cover the methods necessary to determine value.

III. THE ELEVENTH CIRCUIT'S ABSURD APPLICATION OF THE CLEAR STATEMENT RULE WOULD JEOPARDIZE MANY OTHER FEDERAL STATUTORY PROVISIONS GOVERNING STATE AND LOCAL TAX.

The Eleventh Circuit's broad application of the clear statement rule could jeopardize many other federal statutory provisions governing state and local tax. As seen above, the Eleventh Circuit's approach to the clear statement rule requires that Congress spell out every variable, every possibility, and every nuance of the unlimited variety of possible challenges under the 4-R Act or those challenges will be found to be disallowed by the clear statement rule. This overly strict approach, if applied to other federal legislation impacting state and local tax, could undermine the entire purpose behind such legislation. The clear statement rule should be applied cautiously lest it destroy the intent of Congressional legislation meant to solve significant problems in the state and local tax arena.

Congress has, serving in its role as the protector of interstate commerce, intervened in the world of state taxation numerous times to protect, clarify, and foster uniformity in state tax treatment of multistate transactions and enterprises. These legislative inroads on state sovereignty are limited to circumstances where Congress has heard repeatedly from national stakeholders that the problems existing in our subnational tax structure require a federal solution. Some of the examples of federal legislation that could be eviscerated by the Eleventh Circuit's broad application of the clear statement rule include:

Discriminatory Airline Taxation

This statute prohibits states from levying or collecting a tax on "(1) an individual traveling in air commerce; (2) the transportation of an individual traveling in air commerce;

(3) the sale of air transportation; or (4) the gross receipts from that air commerce or transportation." 49 U.S.C. § 40116(b). The statute also adopts language identical to the prohibition against discrimination found in the 4-R Act. The statute prohibits states from the following acts based on a conclusion that these acts unreasonably burden and discriminate against interstate commerce. States are not permitted to:

> (i) assess air carrier transportation property at a value that has a higher ratio to the true market value of the property than the ratio that the assessed value of other commercial and industrial property of the same type in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
>
> (ii) levy or collect a tax on an assessment that may not be made under clause (i) of this subparagraph.
>
> (iii) levy or collect an ad valorem property tax on air carrier transportation property at a tax rate greater than the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.
>
> (iv) levy or collect a tax, fee, or charge, first taking effect after August 23, 1994, exclusively upon any business located at a commercial service airport or operating as a permittee of such an airport other than a tax, fee, or charge wholly utilized for airport or aeronautical purposes.

49 U.S.C. § 40116(2)(A).

The language of § 40116(2)(A)(i) is identical to the language at issue in this case under § 11501(b)(1). A ruling in this case will therefore impact the protections Congress afforded airline property under § 40116.

Discriminatory Motor Carrier Taxation

In 1980 Congress adopted language identical to the language of § 11501(b) to protect motor carrier transportation

property from discriminatory taxation. Like § 11501(b), the motor carrier statute prohibits the following acts as discriminatory and burdening interstate commerce.

> (1) Excessive valuation of property.—Assess motor carrier transportation property at a value that has a higher ratio to the true market value of the motor carrier transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
>
> (2) Tax on assessment.—Levy or collect a tax on an assessment that may not be made under paragraph (1).
>
> (3) Ad valorem tax.—Levy or collect an ad valorem property tax on motor carrier transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.

49 U.S.C. § 14502.

The motor carrier provision also allows taxpayers access to the federal district court. A ruling in this case will therefore impact the protections Congress afforded motor carrier transportation property under § 14502.

Employee Retirement Income Security Act

Congress broadly preempted state laws taxing employee benefit plans. 29 U.S.C. § 1001 et seq.

Taxation of Energy Generation

Congress preempted state taxes on or with respect to the generation or transmission of electricity if such tax discriminates against out-of-state manufacturers, producers, wholesales, retailers or consumers of that electricity. The provision does not create federal court review but specifies that a tax is discriminatory if it results, either directly or indirectly, in a greater tax burden on electricity which is generated and

transmitted in interstate commerce than on electricity which is generated and transmitted in intrastate commerce. 15 U.S.C. § 391. *See, Arizona Public Service Co. v. Snead*, 441 U.S. 141 (1979), to compare this Court's analysis of § 391 with the Eleventh Circuit's analysis of 49 U.S.C. § 11501(b) in the present case.

Taxation of Outer Continental Shelf Activities

Congress adopted a broad protection of oil and gas companies from state taxation of their activity on the Outer Continental Shelf. The statute says simply that "State taxation laws shall not apply to the Outer Continental Shelf." 43 U.S.C. § 1333(a)(2).

Prohibition of Superfund Taxes

Congress preempted state taxes whose purpose was to provide "compensation for claims for any costs of response or damages or claims which may be compensated under [the Federal Comprehensive Environmental Response, Compensation, and Liability Act]." 42 U.S.C. § 9614(c).

Prohibition of Income Taxes

Congress preempted state income taxes on companies whose sole activity in a state is the solicitation for sales of tangible personal property. 15 U.S.C. § 381.

Taxation of Stock Transfers

Congress preempted state taxation of change in beneficial or record ownership of securities when such state taxation was asserted based on the physical location of the agent handling the transfer. 15 U.S.C. § 78bb(d).

Taxation of Satellite Service

Congress prohibited local tax jurisdictions from imposing tax on providers of direct-to-home satellite services. 47 U.S.C. § 251 et seq.

Taxation of Passengers on Motor Carrier

Congress prohibited states from imposing tax on interstate passenger transportation by motor carrier. 49 U.S.C. § 14505.

Taxation of Internet Access

Congress prohibited states from imposing tax on internet access charges. 47 U.S.C. § 151 note.

Mobile Telecommunications Sourcing

Congress established uniform nationwide sourcing rules for state and local taxation of mobile telecommunications services. 4 U.S.C. §§ 116-126.

Each of these statutory provisions reflects a Congressional intent to protect interstate commerce from undue burdens and from discriminatory taxation. Unless the Eleventh Circuit's decision is corrected, each of these statutory provisions could be subject to unexpected litigation seeking to limit the impact of Congressional action by applying the Eleventh Circuit's overly-strict clear statement rule.

In addition to the existing laws identified above, numerous bills are pending in Congress which would be subject to the intense scrutiny of the Eleventh Circuit's clear statement rule. These bills have been drafted with the understanding that it is not necessary for Congress to expressly describe every possible means the states could use to circumvent the purpose of the bill. Without relief from the Eleventh Circuit's holding, the drafting of each of these bills would need to be evaluated.

Legislation has been introduced which seeks to prohibit states from imposing business activity taxes on companies that do not have a certain level of physical presence in the state. Business Activity Simplification Act of 2007, S. 1726, 110th Cong., 1st Sess. (2007).

Legislation has been introduced which seeks to establish standards under which states could require remote sellers to collect sales and use tax on sales into the state and which creates jurisdiction in the Court of Federal Claims to hear certain disputes arising under the legislated standards. Sales Tax Fairness and Simplification Act, S. 34, 110th Cong., 1st Sess. (2007).

Legislation has been introduced which would impose a three-year moratorium on new, discriminatory state or local taxes on cell phone services, property or providers. Cell Phone Tax Moratorium Act of 2007, S. 166, 110th Cong., 1st Sess. (2007).

Legislation has been introduced which would adopt language identical to that of the 4-R Act respecting discrimination against natural gas pipeline property values. The legislation would also create jurisdiction in the district courts to hear disputes. To Prevent Certain Discriminatory Taxation of Natural Gas Pipeline Property, H.R. 2230, 110th Cong., 1st Sess. (2007).

Legislation has been introduced which would authorize the states to provide certain tax incentives to any person for economic development purposes. Economic Development Act of 2007, S. 914, 110th Cong., 1st Sess. (2007).

State discrimination against interstate businesses is a growing problem for businesses struggling to compete in an increasingly competitive global business environment. The result has been an increasing cry for federal legislation establishing uniform rules and protections for commerce among the states. The question raised by the present case is quite simply, how specific does Congress have to be when it legislates to protect interstate commerce from antiquated and discriminatory local tax laws? While that question may not be susceptible to a precise answer, it is perfectly clear that Congress's prohibition on discrimination based on true mar-

ket value is more than specific enough to require a district court to hear evidence relevant to the proper methodology to use in making that valuation.

CONCLUSION

The 4-R Act sets forth prohibitions on discrimination and an avenue for relief in federal court that were intended to relieve railroad property from acts of discriminatory taxation by state and local governments. For Congress' words to have meaning, taxpayers must have the ability to challenge state discrimination whether it is accomplished by tax rate or assessment methodology. To hold otherwise eviscerates the purpose of the 4-R Act and jeopardizes the legitimacy of numerous other federal Acts impacting state and local taxation.

RELIEF REQUESTED

The Council On State Taxation respectfully requests that this Court reverse the decision of the Eleventh Circuit.

Respectfully submitted.

STEPHEN P. KRANZ *
DOUGLAS L. LINDHOLM
JANA MALONE
BOBBY L. BURGNER
J. HUGH MCKINNON
COUNCIL ON STATE TAXATION
122 C Street, N.W., Suite 330
Washington, D.C. 20001
(202) 484-5221

* Counsel of Record

No. 06-1287

IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.

Petitioner,

v.

STATE BOARD OF EQUALIZATION OF THE STATE OF GEORGIA; BART L. GRAHAM, AS COMMISSIONER OF REVENUE OF THE STATE OF GEORGIA; RUSSELL W. HINTON, AS STATE AUDITOR OF THE STATE OF GEORGIA; AND GENA L. ABRAHAM, AS DIRECTOR OF THE GEORGIA STATE PROPERTIES COMMISSION,

Respondents.

On Writ of Certiorari
To the United States Court of Appeals
for the Eleventh Circuit

BRIEF OF MULTISTATE TAX COMMISSION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

Shirley K. Sicilian, General Counsel
Bruce J. Fort, Counsel
Sheldon H. Laskin, Counsel of Record
Multistate Tax Commission
444 No. Capitol St., N.W., Suite 425
Washington, D.C. 20001-1538
(202) 624-8699

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BRIEF OF MULTISTATE TAX COMMISSION as *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS[1]

INTEREST OF *AMICUS CURIAE*

Amicus curiae Multistate Tax Commission (Commission) files this brief in support of the Georgia State Board of Equalization and its individual members, including the State Revenue Commissioner (State). The Commission agrees with the State that Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 (4-R Act or the Act), currently codified at 49 U.S.C. § 11501, does not give federal district courts jurisdiction to review a state's choice of reasonable methodology for estimating "true market value" of railroad property.

The Commission is the administrative agency for the Multistate Tax Compact (Compact), which became effective in 1967. *See* RIA All States Tax Guide ¶ 701 *et seq.*, (2005). Today, forty-seven states and the District of Columbia are members of the Commission. Twenty have legislatively established full membership. Seven are sovereignty members and twenty-one are associate members.[2] This Court upheld

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[1] No counsel for any party authored this brief in whole or in part. Only *amicus* Multistate Tax Commission and its member states through the payment of their membership fees made any monetary contribution to the preparation or submission of this brief. This brief is filed by the Commission, not on behalf of any particular member state. Finally, this brief is filed with the consent of the parties.

[2] Compact Members: Alabama, Alaska, Arkansas, California, Colorado, District of Columbia, Hawaii, Idaho, Kansas, Michigan, Minnesota, Missouri, Montana, New Mexico, North Dakota, Oregon, South Dakota, Texas, Utah and Washington. Sovereignty Members: Georgia, Kentucky, Louisiana, Maryland, New Jersey,

the validity of the Compact in *United States Steel Corp.* v. *Multistate Tax Comm'n*, 434 U.S. 452 (1978).

The purposes of the Compact are to: (1) facilitate proper determination of State and local tax liability of multistate taxpayers, including equitable apportionment of tax bases and settlement of apportionment disputes, (2) promote uniformity or compatibility in significant components of tax systems, (3) facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration, and (4) avoid duplicative taxation. *See* Compact, Art. I. These purposes are central to the very existence of the Compact, which was the states' answer to an urgent need for reform in state taxation of interstate commerce. *See e.g.*, H.R. Rep. No. 89-952, Pt. VI, at 1143 (1965). If the states failed to act, Congress stood ready to impose reform itself through federal legislation that would preempt and regulate state taxation.[3]

The promise of increased uniformity established by the states' adoption of the Compact was critical to preserving the recognized sovereignty the States enjoyed, and continue to

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West Virginia and Wyoming. Associate Members: Arizona, Connecticut, Florida, Illinois, Iowa, Indiana, Maine, Massachusetts, Mississippi, Nebraska, New Hampshire, New York, North Carolina, Ohio, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Tennessee, Vermont and Wisconsin.

[3] The Willis Committee, a congressional study of state taxation mandated by Title II of Pub. L. No. 86-272, 73 STAT. 555, 556 (1959), made extensive recommendations as to how Congress could regulate state taxation of interstate and foreign commerce. *See generally Interstate Taxation Act: Hearings on H.R. 11798 and Companion Bills Before Special Subcomm. on State Taxation of Interstate Commerce of the House Comm. on the Judiciary*, 89th Cong., 2d Sess. (1966).

enjoy, with respect to taxation of interstate commerce. Preserving state tax sovereignty under our vibrant federalism remains a key purpose of the Commission.

The importance the Commission attaches to the present case, and our motivation in filing this brief, lies in this goal of preserving states' authority to determine their own tax policies within federal constitutional and statutory limitations, and in protecting that authority from federal interference beyond that clearly mandated by Congress. The Commission agrees with the State of Georgia, the Fourth Circuit Court of Appeals and the Eleventh Circuit Court of Appeals, that Congress has not clearly expressed an intent in the 4-R Act to interfere with a state's exercise of sovereignty by subjecting its choice of a reasonable property valuation methodology to review in federal district courts. *See Chesapeake Western Ry.* v. *Forst*, 938 F.2d 528 (4th Cir. 1991), *cert. den.*, 503 U.S. 966 (1992); *CSX Transportation, Inc.* v. *State Bd. of Equalization*, 472 F.3d 1281 (11th Cir. 2006). The Petitioner's expansive interpretation of the federal courts' powers under the Act would result in unnecessary and burdensome interference with state sovereignty in violation of federalist principles.

SUMMARY OF THE ARGUMENT

A State's choice of methodology for estimating true market value of property is an important component of its fundamental power to tax. Legislative history surrounding the adoption of the 4-R Act suggests Congress was well aware of the role of states' valuation methodologies in determining effective assessment ratios for railroad property, and of the importance of this policy choice to the States. Yet, there is no mention of pre-emption, or of explicit grant of federal district court authority to review these important methodologies,

in the language of the Act. Had Congress intended to interfere with state's tax sovereignty in choosing reasonable valuation methodologies for railroads, it would have spoken with clarity and precision. In the absence of such clarity, principles of federalism compel the finding that a state's choice of reasonable valuation methodology should not be subject to review and potential revision in federal district courts.

ARGUMENT

PRINCIPLES OF FEDERALISM COMPEL AGAINST A BROAD CONSTRUCTION OF THE ACT WHICH WOULD ALLOW FEDERAL DISTRICT COURT REVIEW OF A STATE'S CHOICE OF RAILROAD PROPERTY VALUATION METHODOLOGY

The federal Tax Injunction Act, 28 U.S.C. § 1341, prohibits federal district court interference with matters of state taxation where a "plain, speedy and efficient" remedy exists in state court. The 4-R Act provides a limited exception to the Tax Injunction Act. 49 U.S.C. § 11501. Specifically, subsection (c) of §11501 of the 4-R Act allows federal district court review where necessary to prevent a State from committing any one of four acts deemed to "unreasonably burden and discriminate against interstate commerce...." with respect to railroads. The 4-R Act does not allow federal district court review of *any* state action that arguably could constitute discrimination against railroads in some form,[4] but

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[4] Other enactments of Congress contain broader language prohibiting States from taxing a particular activity or industry differently or at all. *Cf.*, 15 U.S.C. § 391, regarding taxation of energy generation; 43 U.S.C.

instead allows review only of those actions enumerated in subsection (b) of §11501. *See Department of Revenue of Oregon* v. *ACF Industries, Inc.*, 510 U.S. 332 (1994) (4-R Act does not limit states' discretion to exempt non-railroad property, but not railroad property, from generally applicable *ad valorem* property taxes.)

In this case, CSX Transportation, Inc. (Petitioner) alleges the State violated subsection (b)(1) of the 4-R Act by assessing railroad property at a ratio to true market value that was higher than the ratio used to assess other commercial and industrial property. Under subsection (b)(1), a State may not:

> *assess* rail transportation property at a value that has a *higher ratio* to the true market value of the rail transportation property *than the ratio* that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.

49 U.S.C. § 11501(b)(1)

Georgia's statutes do not present a facial violation of subsection (b)(1): the assessment ratio for both types of property is set at 40% of true market value. Code of Georgia, § 48-5-7(a) (1981). Nonetheless, Petitioner argues that the effective assessment ratio for railroad property is higher than the statu-

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§ 1333(a)(2), regarding taxation of outer-continental shelf activity; 47 U.S.C. § 151 Notes, regarding moratorium on internet taxes.

torily-prescribed ratio, and thus higher than the assessment ratio for other commercial and industrial (C&I) property, in violation of subsection (b)(1). According to the Petitioner, the effective assessment ratio for railroad property is higher than the statutory ratio because the state's valuation methodology produces a higher estimate of true market value than that produced by Petitioner's own proposed methodology. Brief of Petitioner, pp. 16 -17.

Thus, this case raises the question left unanswered in *Burlington Northern Railway Co.* v. *Oklahoma Tax Comm'n,* 481 U.S. 454 (1987), namely, whether a taxpayer may challenge a state's effective assessment ratio in federal district court by substituting the taxpayer's own methodology for estimating true market value in place of the state's reasonable methodology. As a matter of statutory interpretation, informed by principles of federalism, the answer should be "no."

The Commission respectfully suggests this conclusion flows from this Court's reasoning in *Department of Revenue of Oregon* v. *ACF Industries, Inc.*, 510 U.S. 332 (1994). Though the issue before the Court in *ACF Industries, Inc.* concerned the permissibility of property tax exemptions under subsection (b)(4) of the 4-R Act, and its holding was based first upon a statutory construction of the Act which does not apply here, the Court also found:

> Principles of federalism support, in fact compel, our view. Subsection (b)(4), like the whole of [49 U.S.C. § 11501], sets limits upon the taxation authority of state government, an authority we have recognized as central to state sovereignty. (citations omitted) When determining the breadth of a federal statute that impinges

> upon or pre-empts the States' traditional powers, we are hesitant to extend the statute beyond its evident scope. (citations omitted). We will interpret a statute to pre-empt the traditional state powers only if that result is 'the clear and manifest purpose of Congress.' (citation omitted).

510 U.S. at 345.

In applying these federalist principles, the *ACF* Court took into consideration that (1) the particular aspect of state taxation at issue in that case (property tax exemptions) reflected important state tax policies which pre-dated the 4-R Act, and (2) Congress made no expression of intent to limit the states' allowance of such exemptions either in the language of the statute or in its legislative history. 510 U.S. at 344-345. Each of these considerations is equally present with respect to a state's choice of property tax valuation methodology, and the application of federalist principles is no less compelling in the present case.

I. The Methodology for Estimating True Market Value of Railroad Property is an Important State Tax Policy Choice.

The proposition that a state's ability to raise revenue through taxation embodies a core sovereignty value is beyond dispute. This Court has consistently recognized that the states' taxing powers provide a crucial component of sovereignty necessary to support our federal system. *National Private Truck Council, Inc.* v. *Oklahoma Tax Comm'n*, 515 U.S. 582, 586 (1995), quoting *Dows* v. *City of Chicago*, 11 Wall. 108, 110 (1871) ("It is upon taxation that the several States chiefly rely to obtain the means to carry on their re-

spective governments, and it is of the utmost importance to all of them that the modes adopted to enforce the taxes levied should be interfered with as little as possible."); *Wisconsin* v. *J.C. Penney Co.*, 311 U.S. 435, 444 (1941) ("[The Constitution] does not demand of states strict observance of rigid categories nor precision of technical phrasing in their exercise of the most basic power of government, that of taxation.") Without that power, States will either have to forgo providing residents with needed services and protections or be relegated to a dependency upon the federal government.

A state's choice of reasonable valuation methodology is an important component of this fundamental power to tax. *See Louisville & Nashville R.R. Co.* v. *Dep't of Revenue, Fla.*, 736 F.2d 1495, 1498 (11th Cir. 1984) ("These arguments broach delicate issues implicating the State's traditional authority to select methods of valuation.") The Fourth Circuit acknowledged the importance of this choice to States and characterized a federal court review aimed at choosing among competing methodologies to produce a "true market value" as a "difficult, and arguably impossible task" which would "completely displac[e] the fact-finding and policy-making powers of state government." *Chesapeake Western Railway Co.*, 938 F.2d at 533. Indeed, some States have codified this policy choice in their statutes. *See, e.g.*, Ark. Stat. Ann. § 26-26-1607 (1987); Ala. Code § 40-21-6 (1975); Colo. Rev. Stat. § 39-4-102 (1999); and Fla. Stat. § 193.011 (2006). Petitioner's reading of the 4-R Act would make these legislative choices essentially meaningless for valuing railroad property.

The decision in *Union Pacific Railroad Co.* v. *State Tax Comm'n of Utah*, 716 F. Supp. 543 (D. Utah 1988), underscores the important policy nature of a State's choice of valuation methodologies, and explains why that choice

should be respected absent some evidence that the methodology was irrational. Following a valuation trial under the 4-R Act which lasted some six weeks, including 17 days of expert testimony on competing valuation methodologies, *id.* at 547, the district court stated its belief that a court could not empirically chose the best valuation methodologies, and should concern itself simply with determining whether the state's selected methodology is reasonable:

> From the beginning of this case, the court was willing to assume that there was such a thing as a "true market value" that could be determined objectively from evidence much the same way a court can determine a wrongfully discharged employee's back wages from evidence (citation omitted). ...
>
> From the six weeks of testimony in this case, however, certain things became apparent. ....
>
> From all the evidence presented it is clear there is more than one way to value a railroad. (citations omitted). Each method may represent what some buyers and sellers may actually do. All of the methods may be equally rational given their underlying assumptions....Each method or theory depends on certain assumptions that cannot ultimately be proved or disproved by reason alone nor replicated in experience. *Thus, this court cannot say that any one method is necessarily more rational than any other.*
>
> ....
>
> If one has a choice of methods and chooses a method with a rational footing and is consistent and even-handed in applying the

> method to all comparable properties, then conceptually the end result should be payment by taxpayers of a tax bill that is not disproportionate to the like payment of all other comparable taxpayers.

716 F. Supp. at 554-5, 556-7 (emphasis added); *See also, Chesapeake Western*, 938 F.2d at 531 ("The concept of true market value is inherently an approximation, in some sense a fiction, since there is no such thing as a perfect market. This is particularly true of railroad land...").

The deference accorded by this Court to a state's choice of formulary apportionment methodologies for income tax purposes presents an analogous situation, given the difficulty of arriving at a "true" income figure and the shared conceptual foundation of formulary apportionment of income and property tax jurisprudence. In *Underwood Typewriter Co.* v. *Chamberlain*, 254 U.S. 113 (1920), this Court considered whether Connecticut's apportionment of a taxpayer's net income was discriminatory. The Court first recognized the analogy to property tax and held "[a] tax is not obnoxious to the commerce clause merely because imposed upon property used in interstate commerce ... (citations omitted) whether it be deemed a property tax or a franchise tax," *id.* at 119-120, then went on to find that the state's choice of apportionment formula must be upheld unless it is "inherently arbitrary" or produces an "unreasonable result":

> The legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It, therefore, adopted a method of apportionment

> which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the state. 'The plaintiff's argument on this branch of the case,' as stated by the Supreme Court of Errors, 'carries the burden of showing that 47 per cent. of its net income [the amount that resulted from the State's formulary calculation] *is not reasonably attributable*, for purposes of taxation, to the manufacture of products from the sale of which 80 per cent. of its gross earnings was derived after paying manufacturing costs.' The corporation has not even attempted to show this... There is, consequently, nothing in this record to show that the method of apportionment adopted by the state was *inherently arbitrary* (footnote omitted), *or that its application to this corporation produced an unreasonable result.*

254 U.S. at 121 (emphasis added).

This Court's more recent income tax decisions are consistent with *Underwood Typewriter*. They recognize the importance of a state's choice of formulary apportionment methodologies and have upheld them despite their inherent nature as approximations and the impossibility of demonstrating that those formulas produce precise apportionment of income. For example, in *Moorman Manufacturing* v. *Bair*, 437 U.S. 267 (1978), the Court noted:

> The single factor formula used by Iowa, therefore, generally will not produce a figure that represents the actual profits earned within the State. But the same is true of the Illinois three-factor formula. Both will occasionally over-

> reflect or under-reflect income attributable to the taxing State. Yet despite this impression, the Court has refused to impose strict constitutional restraints on a State's selection of particular formula. (footnote omitted).

437 U.S. at 273; *See also, Mobil Oil* v. *Vermont,* 445 U.S. 425 (1980) (declining to limit state methods for sourcing income from dividends); *Container Corporation of America* v. *Franchise Tax Board,* 463 U.S. 159 (1983) (rejecting claim that California's apportionment formula distorted the profitability of the taxpayer's foreign operations where evidence was based on different accounting methodology).

Clearly, this Court has recognized the vital importance to States of upholding their ability to adopt reasonable formulas for estimating various forms of taxpayer value where it would be impossible to say objectively that any one formula produces the most accurate result. The alternative would be a free-for-all process where federal courts would be forced to make quasi-legislative policy choices between competing reasonable accounting methodologies.[5]

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[5] In the analogous context of rate-making, this Court held in *Colorado Interstate Gas Company* v. *Federal Power Commission,* 324 U.S. 581 (1945):

> Rate-making is essentially a legislative function. (citation omitted). When Congress, as here, fails to provide a formula for the Commission to follow, courts are not warranted in rejecting the one which the Commission employs unless it plainly contravenes the statutory scheme of regulation.

324 U.S. at 589.

II. Neither the Language of the Act, Nor Its Legislative History, Indicates Congressional Intent to Interfere With This Important State Policy Choice by Allowing Federal District Court Review.

In the years prior to the enactment of the 4-R Act, many States, by statute or constitution, classified railroad property separately from other commercial and industrial property, and imposed a higher assessment ratio on that railroad classification than on the commercial and industrial class. *See Nashville, Chattanooga & St. Louis Ry.* v. *Browning*, 310 U.S. 362 (1940) (States were permitted to classify carrier property in a separate class from other taxable property in the same jurisdiction.).

The often-referenced "Doyle report", S. Rep. No. 87-445 (1961), characterized this separate classification of railroad property as "a studied and deliberate practice of assessing railroad property as a proportion of full value substantially higher than other property." *Id.* at 458. Although, as Petitioner points out, some federal and state courts had "voided discriminatory tax assessments and levies on common carrier property" through express state-law protections or amendments, those protections did "not reach the situation . . .where the express provisions of State law or a State constitution permit such discriminatory treatment." S. Rep. No. 90-1483, at 6-7 (1968). Congress recognized that protections for railroads were limited absent remedial federal legislation and concluded "such discrimination must be ended." S. Rep. No. 92-1085, at 7 (1972). *See* Brief of Petitioner, pp. 3-4.

There is no doubt Congress accomplished this particular goal in subsection (b)(1) of the 4-R Act which clearly prohibits a State from imposing an assessment ratio for railroads

that is higher than the assessment ratio imposed on other commercial and industrial property, whether by state statute or constitution. Nor did Congress leave any doubt that subsection (c) of the Act allows federal district court review to prevent a facial violation of subsection (b)(1).

It is also clear that Congress intended federal district court review pursuant to subsection (c) to go beyond facial assessment ratios and include effective assessment ratios. Certainly, subsection (c) allows federal district courts to consider the effective aggregate assessment ratio for commercial and industrial property by testing the accuracy of state valuations of that property, in the aggregate, through the use of a sales ratio study (a study that compares sale prices of various commercial and industrial properties to the state's previous estimates of the value of those properties). Furthermore, this Court has found that the language of subsection (c) allows federal district courts to compare this effective aggregate C&I assessment ratio to the effective assessment ratio for a particular taxpayer's railroad property by considering the factual determinations to which the state's preferred railroad valuation methods were applied in a particular case. *Burlington No. R. Co.* v. *Okla. Tax Comm'n,* 481 U.S. at 462-3.

What is not clear under either subsection (b)(1) or subsection (c) is whether federal district court review of effective assessment ratios for individual railroads includes not just a review of the application of the State's reasonable valuation methodology, but also a review of that methodology itself. In fact, this Court has expressly noted, but reserved judgment, on that issue. *Id.* at 463, n.5.

At the time of the 4-R Act's enactment, Congress was clearly aware of the role of states' valuation methodologies in determining effective assessment ratios, and of the impor-

tance of this policy choice to the States. Not only did the Doyle report provide significant explanatory background on the various different methodologies used by states in valuing railroad property, S. Rep. No. 87-445, at 452-59, 475-81, it also expressed the opinion that discrimination against railroads "results" in large measure from "outmoded assessing procedures" employed at the state level. *Id.* at 448. It contended that "the applicable [state] statutes contain few guideposts for the assessor or prescription of the factors, and the weight to be accorded thereto, in arriving at 'full value' of railroad—or any other—real estate," and railroad property is "often valued under divergent theses, processes and procedures and too often inconsistently from year to year." *Id.* at 568. *See also* Brief of Petitioner, p. 36.

Despite the information and opinions contained in the Doyle report, Congress did not see fit to remedy that situation by pre-empting the states' choice of valuation methodology in subsection (b), nor is there any explicit grant of federal district court authority to review these methodologies in subsection (b)(1) or (c).

Indeed, legislative history provides some indication that Congress consciously intended *not* to interfere with States' choice of railroad valuation methodology. In S. Rep. No. 90-1483, the Senate Committee on Commerce stated its intent that the term "true market value" as used in the bill under consideration (S. 927), should have the meaning set forth in "Appendix B," which provided:

> [The bill] does not suggest or require a State to change its assessment standards, assessment practices, or the assessments themselves. It merely provides a single standard against which all affected assessment must be measured in or-

> der to determine their relationship to each other. It is not a standard for determining value; it is a standard to which values that have already been determined must be compared.

S. Rep. No. 90-1483, App. B (1968)[6]

In *Chesapeake Western*, the Court noted the testimony of a railroad executive on another earlier version of Section 11501 stating:

> The standards and methods of valuation that any State wishes to use would be totally unaffected by this legislation. H.R. Rep. 91-138 (1970) (statement of Philip Lanier).

938 F.2d at 531.

Despite the legislative history contained in the Doyle report indicating that Congress was well aware of the importance, role and then-current status of state valuation methodologies, nowhere in the Act does Congress plainly express any intent to displace these methodologies, either by direct federal pre-emption or by allowing federal district

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[6] As noted by the Court in *Louisville & Nashville R.R. Company* v. *Dep't of Revenue, Fla.*:

> [W]ith the passage of the 4R Act, Congress capped a seventeen-year effort to equalize railroad property taxes. S. 927, one of several precursors, was virtually a mirror image of section 11503 [now 11501]. The legislative history of nearly identical antecedent proposals is unquestionably relevant and material to a complete understanding of the text before the court. (citation omitted).

736 F.2d 1495, 1498, n.6.

court review in contravention of the Tax Injunction Act. On the contrary, the absence of any language expressly addressing state railroad valuation methodologies, and statements in the legislative history assuring those methodologies were left unaffected, indicate Congress ultimately concluded, despite the Doyle report's criticisms, to forgo interfering with states' choice of reasonable railroad valuation methodology.

III. Where Congress Has Not Expressed an Intent to Allow Federal District Court Review of an Important State Policy Choice, Principles of Federalism Compel Against Allowing Such Review.

It is a cornerstone of our federalist system that Congressional intent to pre-empt state tax sovereignty must be made clear and explicit. *See ACF Industries, Inc.*, 510 U.S. at 345, ("We will interpret a statute to pre-empt the traditional state powers only if that result is the 'clear and manifest purpose of Congress.'" *quoting from, Rice* v. *Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947).). As this Court stated in *Cipollone* v. *Liggett Group, Inc.*, 505 U.S. 504 (1992):

> The principles of federalism and respect for state sovereignty that underlie the Court's reluctance to find preemption where Congress has not spoken directly to the issue apply with equal force where Congress has spoken, though ambiguously. In such cases, the question is not *whether* Congress intended to pre-empt state regulation, but to what *extent*. We do not, absent unambiguous evidence, infer a scope of pre-emption beyond that which clearly is mandated by Congress' language.

505 U.S. at 533. *See also, Gregory* v. *Ashcroft*, 501 U.S. 452 (1991) (clear or plain statement rule applied).

As *ACF Industries, Inc.* illustrates, the doctrine that state preemption will be found only where clearly and manifestly expressed applies firmly in the field of state taxation. Had Congress intended to interfere with the important, pre-existing, state authority to choose reasonable valuation methodologies for railroads, "we are confident it would have spoken with clarity and precision." 510 U.S. at 344. In the absence of such clarity, principles of federalism compel the finding that a State's choice of reasonable valuation methodology should not be subject to review and potential substitution with alternative methodologies.

CONCLUSION

The Commission respectfully counsels that the decision of the Eleventh Circuit Court of Appeals in this case be upheld.

Respectfully submitted,

Shirley K. Sicilian, General Counsel
Bruce J. Fort, Counsel
Sheldon H. Laskin, Counsel of Record
Multistate Tax Commission
444 No. Capitol St., N.W., Suite 425
Washington, D.C. 20001-1538
(202) 624-8699

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IN THE

Supreme Court of the United States

CSX TRANSPORTATION, INC.,

Petitioner,

v.

GEORGIA STATE BOARD OF EQUALIZATION, ET AL.,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

BRIEF OF THE TAX FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

CHRISTOPHER D. ATKINS
Senior Tax Counsel
TAX FOUNDATION
2001 L Street NW,
Suite 1050
Washington, DC 20036
(202) 464-6200

BRIAN E. BAILEY*
**Counsel of Record*
ICE MILLER LLP
One American Square
Suite 3100
Indianapolis, IN 46282
(317) 236-2426

WILSON-EPES PRINTING CO., INC. - (202) 789-0096 - WASHINGTON, D.C. 20002

QUESTION PRESENTED

Whether, under the federal statute prohibiting state tax discrimination against railroads, 49 U.S.C. § 11501(b)(1), a federal district court determining the "true market value" of railroad property must accept the valuation method chosen by the State.

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BRIEF OF THE TAX FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

INTEREST OF THE *AMICUS CURIAE*

The Tax Foundation submits this brief as *amicus curiae* in support of Petitioner in the above-captioned matter.[1]

The Tax Foundation is a non-profit research organization founded in 1937 to educate the public about

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[1] No counsel for a party authored this brief in whole or in part, and no person or entity, other than *amicus curiae*, has made a monetary contribution to the preparation or submission of this brief. Written consent of the Petitioner and Respondent have been obtained and filed with the Clerk of the Court.

sound tax policy. To this end, we disseminate information on taxes and promote tax systems that are simple, fair, and conducive to economic growth. The Tax Foundation works to further this mission by educating the legal community on issues relating to tax law, by explaining tax law concepts to lawmakers and the public in an understandable and relevant manner, and by advocating that judicial decisions on tax law promote principled tax policy. Accordingly, the Tax Foundation has a direct stake in the outcome of this case.

SUMMARY OF ARGUMENT

The Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act" or "the Act") allows federal courts to hear challenges to a state's property tax assessment method with regard to railroads. Congress authorized such challenges, when it approved the 4-R Act, not merely to rescue a troubled industry, but also to protect the right of railroads to be free from discriminatory state and local taxation.

The courts below are in error insofar as they held that taxpayers may only challenge the application of an assessment method and not the method itself. This interpretation contravenes the Act's textual command to consider a property's *"true* market value," not just one party's estimation of that value. Such challenges are vital to give effect to the Act.

More broadly, this Court should not insulate assessment methods from challenge where Congress has demonstrated a desire to protect interstate commerce. Ensuring a transparent process, with the goal of determining *"true* market value," is the best way to protect interstate commerce and individual rights, and uphold the text, purpose, and meaning of the 4-R Act.

ARGUMENT

I. TO PROTECT INTERSTATE COMMERCE AND INDIVIDUAL RIGHTS, THE 4-R ACT ALLOWS FEDERAL COURTS TO HEAR CHALLENGES TO A STATE'S USE OF A PARTICULAR TAX ASSESSMENT METHOD.

A. The 4-R Act limited the power of states to tax to discriminate in its tax assessments.

For a number of reasons, American interstate railroads by the 1970's were in "an anemic condition." *United States v. SCRAP*, 412 U.S. 669, 724 (1973) (White, J., dissenting in part). Deterioration in passenger and freight service, and the 1970 bankruptcy of the Penn Central Railroad—the largest corporate bankruptcy in American history at the time—spurred Congress into action. A series of comprehensive federal statutes sought to address the numerous causes of railroads' decline, which included passenger service mandates, calcified rate and regulatory structures, antiquated work rules, and discriminatory state and local property taxes.

State taxation was the focus of Section 306 of the Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act" or "the Act"), now codified at 49 U.S.C. § 11501 *et seq.* (2002). The Act forbids state or local government action to:

> (1) Assess rail transportation property at a value that has a higher ratio to the *true market value* of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the *true market value* of the other commercial property.

> (2) Levy or collect a tax on an assessment that may not be made under paragraph (1) of this subsection.

49 U.S.C. § 11501(b) (2002) (emphasis added). A railroad subject to such discriminatory taxation is entitled to relief as an exception to the Tax Injunction Act, 28 U.S.C. § 1341. *See* 49 U.S.C. § 11501(c).

Thus, rail transportation property may not be assessed for the purposes of state and local taxation at a higher level than other commercial property in the state, nor may it be taxed at a higher level than other commercial property in the state. Just as a state cannot use different methods that have discriminatory effects, neither can it use one method if it has a discriminatory effect. *See CSX Transportation, Inc. v. State Board of Equalization*, 472 F.3d 1281, 1293 (11th Cir. 2006) (Faye, J., concurring in part and dissenting in part) ("Surely a state could not use one method to assess the market value of railroad property and a different method to assess other commercial and industrial property if such [use] resulted in gross discrimination toward the railroad.").

A contrary interpretation of Section 306 would lead to absurd results. For instance, if a state were to calculate property assessment with an odd but conceivably rational method, such as by the ratio of trees on the land to trees on the land of other assessed properties, or by the property's height above sea level, it should not be immune from challenge under the 4-R Act if discriminatory effects resulted from the use of that method.

The Act therefore must permit challenges to state and local property tax assessment method in certain situations. Although states are less constrained in other regulatory contexts by virtue of federalism, Congress has used its plenary power over interstate commerce to limit states' ability to use any conceivable method of assessing

and taxing rail transportation property, in that such methods may be challenged in federal court.

B. The purpose of the 4-R Act is to protect interstate commerce and the right to be free from discriminatory state taxation.

Congress's purpose in enacting the 4-R Act was not merely to rescue a troubled industry as an end in itself. A goal of federal involvement of the railroad industry is "to ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers and with other modes, to meet the needs of the public and the national defense." 49 U.S.C. § 10101(8). The now resuscitated industry is just as vital today. "Freight railroads are critical to U.S. economic health and global competitiveness. They move approximately 40 percent of our nation's freight . . . and connect businesses with each other across the country and with markets overseas." ASSOCIATION OF AMERICAN RAILROADS, OVERVIEW OF U.S. FREIGHT RAILROADS (Jan. 2007), *available at* http://www.aar.org/PubCommon/Documents/AboutTheIndustry/Overview.pdf. Removing burdens on railroads removes burdens on interstate commerce.

The 4-R Act demonstrates awareness that railroads suffered discriminatory taxation as they struggled to survive. "Unfortunately, interstate carriers, especially railroads, are easy prey for State and local tax assessors. Railroads, oil pipelines, and other interstate carriers are nonvoting, often nonresident, targets for local taxation, and cannot easily remove their right-of-way and terminals." Report of the U.S. Senate Committee on Commerce, *Discriminatory State Taxation of Interstate Carriers*, S. REP. NO. 91-630 at 3. Remedying this discrimination not only unburdened interstate commerce, but also protected the rights of the railroads to be free of

discriminatory treatment. "The committee joins the Interstate Commerce Commission in recommending enactment of this legislation to eliminate the discriminatory tax practices weakening our national transportation system and burdening the Nation's consumers." *Id.*

Federal courts should of course seek to balance the powers of the federal government under the Constitution with the powers of state and local governments under their respective constitutions. But when, as in this case, the Constitution has lodged a power in Congress and that body properly chooses to exercise it in such a way as to limit state and local power, federal courts should not show unqualified deference to the interests of state and local governments. To do otherwise is to turn the Constitution on its head.

C. Barring evidence about a state's specific assessment method contravenes the 4-R Act's purpose and text.

Because the key phrase of the statute is "*true* market value," a determination of whether a state assessment method is discriminatory requires a comparison with the actual, real-world market value of the property in question. Discrimination can therefore be found in effects regardless of intentions. *See, e.g., Dep't. of Revenue v. ACF Indus.*, 510 U.S. 332, 350 (1994) (Stevens, J., dissenting) ("[T]he text of [the 4-R Act] and its evident purposes convince me that Congress intended to bar discrimination by any means. . . .") (internal citation omitted).

Both the trial court and the appellate court below held that taxpayers are confined to challenging only the application of a method rather than the method itself—even if it produces discriminatory tax assessments that gave rise to the Act in the first place. *See CSX Transp.*,

472 F.3d at 1290 ("The district court was not allowed to consider a valuation methodology different from the methodology of the Board."); *CSX Transportation, Inc. v. State Board of Equalization*, 448 F. Supp. 2d 1330, 1342 (N.D. Ga. 2005) ("[T]he court concludes that CSXT cannot challenge the Department's chosen valuation methods in this case.").[2]

The Eleventh Circuit interpretation contravenes the Act's textual command to consider a property's "*true* market value," not just one side's estimation of that value. "The language of the statute is straightforward . . . . If the Railroad can prove that the method used by the state does not result in a fair appraisal of true market value and that the assessed value is in fact at a ratio higher than five percent of the ratio of true market value and assessed value of other commercial and industrial property, it is entitled to relief." *CSX Transp.*, 472 F.3d at 1292-94 (Faye, J., concurring in part and dissenting in part). The statute forbids assessments that result in discrimination, and considering evidence about true market value is a prerequisite to determining whether discrimination has occurred. The court below was not only allowed to consider such evidence, it was obligated to do so.

The Eleventh Circuit and the District Court used an inappropriate level of deference to the state government

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[2] In so holding, the Eleventh Circuit reached a conclusion opposite from two sister circuits. *See Burlington N. R.R. v. Dep't. of Revenue*, 23 F.3d 239, 241 (9th Cir. 1994) (holding that state valuation methods may be successfully challenged by "clear, cogent and convincing evidence"); *Consol. Rail Corp. v. Town of Hyde Park*, 47 F.3d 473, 482 (2d Cir. 1995) (holding that railroads can challenge a state's use of a unique assessment method). *But see Chesapeake W. Ry. v. Forst*, 938 F.2d 528, 531 (4th Cir. 1991) (holding that the 4-R Act is ambiguous and does not authorize challenges to assessment methodologies).

in analyzing CSXT's claim of discriminatory treatment. *See id.* at 1288 ("Important questions of state policy are often intertwined with the selection of a valuation method."); *CSX Transp.*, 448 F. Supp. 2d at 1341 ("As long as the Department's chosen valuation methods are rational and were not chosen for the purpose of discriminating against CSXT, the court will not second guess the Department's choice of methods."). The text and purpose of the statute make clear that Congress intended to show no deference to assessment schemes that resulted in discriminatory effects. "In drafting § 11503 [now § 11501], Congress prohibited discriminatory tax rates and assessment ratios in no uncertain terms, and set forth precise standards for judicial scrutiny of challenged rate and assessment practices." *ACF Indus.*, 510 U.S. at 343. Where a taxpayer sees its property tax bill go up 47 percent in one year by a method change, as happened to CSXT in this case, while other taxpayers have only minimal increases, rational basis review is inappropriate under the 4-R Act.

It must be noted that Georgia's method is not enshrined in statute or regulation. *See CSX Transp.*, 472 F.3d at 1293 fn.1 (Faye, J., concurring in part and dissenting in part) (detailing the ad hoc and variable nature of Georgia property tax assessment). Here, the Eleventh Circuit below declined to allow a challenge to the state method in part because the 4-R Act did not provide a "plain statement" permitting interference with state sovereignty. *See CSX Transp.*, 472 F.3d at 1289 ("The text of the Act does not clearly state that railroads may challenge valuation methodologies. Without that clear statement, the argument of the Railroad fails."). Assuming for the moment that the Act is unclear about authorizing interference with state discriminatory assessment practices, a ruling for the petitioner here would not invalidate any Georgia law or regulation. Since the choice of method was made by an employee of the

Department of Revenue and is not bound by law or regulation, the result of those choices should be given *greater* scrutiny under the terms of the Act, not less.

A finding for petitioner in this case would not dictate to states a particular method to use. The record seems to indicate that all methods are but estimations capable of fine-tuning. *See, e.g., CSX Transp.*, 448 F. Supp. 2d at 1340 ("After eight days of trial, it is apparent to the court that valuation is an art, not a science.") Judges should be presented with all available evidence so as to make an informed decision about whether a given method's calculation of "*true* market value" comports with reality and other methods. States would remain free to select any method that meets this statutory requirement. *See* S. REP. NO. 91-630, at 3 (1969) ("The committee wishes to emphasize that this bill would in no way alter the freedom of a State to tax its taxpayers so long as interstate carriers are accorded equal tax treatment with other taxpayers.").

An essential prerequisite to ensuring that rights under the 4-R Act are guaranteed is ensuring the ability to challenge state tax practices, and present evidence on what method ascertains *true* market value. The courts below here have imposed an "absolute preclusion of any challenge to the methodology used by the state. . . ." *CSX Transp.*, 472 F.3d at 1294 (Faye, J., concurring in part and dissenting in part). Such a holding deprives courts of necessary jurisprudential tools and allows states to burden commerce freely in the face of congressional proscription.

D. This Court should not insulate flawed tax assessment methods from challenge.

Ensuring that the process of developing and administering tax systems is subject to open hearings with full opportunity to comment on proposals is a

fundamental principle of sound tax policy. *See* TAX FOUNDATION, TEN PRINCIPLES OF SOUND TAX POLICY, Nos. 9 and 10, *available at* http://www.taxfoundation.org/files/tfprinciples.pdf. Tax legislation should be based on careful economic analysis and transparent procedures. Permitting criticism and challenge can help ensure neutrality, simplicity, and fairness in our tax system.

Railroads are not alone in being subjected to appraisal and assessment disparities that result in discriminatory taxation. In Florida, out-of-state "snowbirds" that own real property in the state are challenging a bifurcated taxation system that imposes higher obligations on them than on in-state residents. *See, e.g.*, Rafael Gerena-Morales, *Florida Snowbirds Challenge Fairness of Two-Tier Tax*, WALL STREET JOURNAL (May 22, 2006), at A1. In June 2007, the Allegheny County, Pennsylvania property tax assessment system was held to violate the state constitution. *See Pierce v. Allegheny County*, No. GD05-028355, slip op. at iv (Allegheny County Court of Common Pleas Jun. 6, 2007) (holding that the use of base year assessments violates the state constitution's uniformity clause). In his opinion, Judge Wettick exhaustively details appraisal methods used by each state in property tax assessment. *See id.* at 52-89. The overview paints a picture of an "administrative process of levying property taxes [that] varies greatly from state to state and even within states." Gerald Prante, *Property Tax Collections Surged with Housing Boom*, TAX FOUNDATION SPECIAL REPORT NO. 146 (Nov. 2006), at 2, *available at* http://www.taxfoundation.org/research/show/2056.html.

That states and localities have different methods of assessment and rates of tax is not inherently discriminatory. Indeed, it is a valued aspect of federalism that local taxes are administered by local governments. *See, e.g., Allied Stores of Ohio v. Bowers*, 358 U.S. 522,

526 (1959) ("When dealing with their proper domestic concerns, and not trenching upon the prerogatives of the National Government or violating the guaranties of the Federal Constitution, the States have the attribute of sovereign powers in devising their fiscal systems to ensure revenue and foster their local interests."). But differences and disparities can cross the line into unlawful discrimination forbidden by the U.S. constitution, state constitutions, and statutes. *See, e.g.*, *id.* at 532 (Brennan, J., joined by Harlan, J., dissenting) ("Because there are 49 States and much of the Nation's commercial activity is carried on by enterprises having contacts with more States than one, a common and continuing problem of constitutional interpretation has been that of adjusting the demands of individual States to regulate and tax these enterprises in light of the multistate nature of our federation."). There are clear limits to the power of the states over individuals, and the 4-R Act is one such limit.

Only by authorizing CSXT and other similarly situated taxpayers the ability to challenge a state's method—and not merely its application—can a court reach a fully-informed decision about *true* market value. Ensuring a transparent process is the best way to protect interstate commerce and individual rights, and uphold the text, purpose, and meaning of the 4-R Act.

CONCLUSION

For the foregoing reasons, *Amicus* respectfully requests that this Court reverse the decision below.

Respectfully submitted,

BRIAN E. BAILEY*
ICE MILLER LLP
One American Square
Suite 3100
Indianapolis, IN 46282
(317) 236-2426

CHRISTOPHER D. ATKINS
Senior Tax Counsel
TAX FOUNDATION
2001 L Street NW,
Suite 1050
Washington, DC 20036
(202) 464-6200

* *Counsel of Record*

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